FTC'S AUTHORITY OVER DECEPTIVE ADVERTISING

HEARING

BEFORE THE

SUBCOMMITTEE FOR CONSUMERS

OF THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION
UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

SECOND SESSION

ON

FTC'S AUTHORITY OVER DECEPTIVE ADVERTISING

JULY 22, 1982

Serial No. 97-134

Printed for the use of the
Committee on Commerce, Science, and Transportation

U.S. GOVERNMENT PRINTING OFFICE
99-520 WASHINGTON : 1982

S261-5

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FTC'S AUTHORITY OVER DECEPTIVE ADVERTISING

THURSDAY, JULY 22, 1982

U.S. SENATE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
SUBCOMMITTEE FOR CONSUMERS,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:20 a.m. in room 235 of the Russell Senate Office Building, Hon. Bob Packwood (chairman of the committee) presiding.

Staff members assigned to this hearing: Lawrence R. Fullerton, Marilyn S. Richmond, and Richard Perlmutter, staff counsels; and Amy L. Bondurant, minority staff counsel.

OPENING STATEMENT BY THE CHAIRMAN

The **CHAIRMAN**. The hearing will come to order, please.

Senator Kasten has had to go to the White House. Senator Cannon and I can stay for most of this hearing. I will go to the Finance Committee for a brief moment when I have to be there for a bill that is being discussed.

Needless to say, the particular issue which we are now going to hear, advertising deception and unfairness, is a controversial issue. Here is my briefing book with the voluminous witness' statements, which I have read in most part.

I want to say to both Chairman Miller and to the Commissioners that I appreciate this issue being raised. It is not an easy issue; it is a complex one. It is one that is arcane; it is one that has a long common law history as well as a long history at the Federal Trade Commission. I know there is disagreement about it, but I do not think that healthy debate is the same as rancorous division. I know that within the Commission there are differences, but I must say to you, Jim, I appreciate your raising the issue.

It is time we had a discussion on deception; it is time we reached some conclusion or agree that we are not going to reach any conclusion. We might as well start the discussion and start the debate, and I hope that these hearings today, if the questions and answers are as revealing as I found the testimony, it is going to be a damn good hearing.

Howard.

Senator **CANNON**. Well, I want to join you in welcoming the Chairman and members of the Commission here to get their views on defining deception.

OPENING STATEMENT BY SENATOR GORTON

Senator GORTON. Mr. Chairman, I am happy to participate in this hearing which you have described as "the first step in a systematic review of the subject (of the FTC's authority over deceptive acts and practices)." I believe we can today sketch the blueprint for a thorough and objective study, "to explore carefully the need for statutory change and the implications of the various proposals"—to quote the committee report on S. 2499.

Frankly, I am convinced that the present language of section 5 of the FTC Act regarding deception has served us very well for over 40 years, and is not in need of repairs. This opinion is based upon my 12 years of experience as Washington State attorney general in enforcing my State's "Baby FTC Act" which prohibits deceptive trade practices in precisely the same language as section 5 does now.

In the case of the section 5 prohibition of deceptive practices, we do not have the same circumstances as we do concerning the prohibition of unfair practices. Proponents of the statutory definition of "unfairness" contained in section 2 of S. 2499 make the rather persuasive argument that this term is so uncertain in scope that some future Federal Trade Commission might be tempted to apply it arbitrarily. By contrast, "deception" has been the subject of a much greater degree of judicial interpretation. From this body of "trade law," developed over many years, has emerged a clear and understandable concept of deceptive trade practices which has proved to be reasonably predictable and quite balanced and workable.

The Commission chairman argues, however, that in the past the Commission has sometimes brought ill-advised cases under the present standard. Although, with all due respect, I believe that many of the cases which Dr. Miller used to illustrate this point in previous hearings before this committee were far more substantial than he implied, I do not doubt that the Commission has occasionally in the past, and may well again in the future, exercise imperfect prosecutorial discretion. But, the various proposed statutory definitions of deception will not prevent this from happening. No statutory definition can substitute for sound prosecutorial judgment. The various proposals will make the "bad cases" more difficult to bring—and to win—by erecting new hurdles for the FTC to clear in filing cases and in satisfying its burden of proof; but it will do the same thing for the good cases. It is far from worth the trade, in my opinion.

With all due respects to the public position of some of the business organizations on this issue, I also believe that these deception proposals are contrary to the interests of the reputable business community. I think so for two reasons. First, by making it more difficult for the FTC to stop deceptive trade practices, these proposals would lead to the result that honest businesses, which do not use such sales techniques, would face increased unfair competition from those unscrupulous businesses which do. Second, as the public perceives that the Government agencies are no longer able to provide sufficient protection against fraud and deception—and my mail indicates that such a perception is already growing—consumer distrust and militancy will increase. We could experience a return to the attitudinal climate in this respect of the late 1960's and early 1970's. This, coupled with the interest rates of the 1980's, would certainly not be beneficial to business. It is precisely for these reasons that we are now experiencing an increasing split within the advertising industry concerning the wisdom of these and other proposals to limit the FTC's suthority over unfair and deceptive acts and practices.

For these reasons, Mr. Chairman, I am pleased to participate in these proceedings. I am convinced that the thorough and objective committee study of this subject, envisioned by your previous statements about the purpose of this hearing, can lead to but one conclusion: The public interest will be best served by leaving the present language of section 5 which prohibits deceptive acts and practices alone; it would be unwise to tinker with this time tested and very successful formula for insuring that our free enterprize system works fairly and properly.

The CHAIRMAN. Mr. Chairman.

STATEMENT OF HON. JAMES C. MILLER III, CHAIRMAN, FEDERAL TRADE COMMISSION

Mr. MILLER. Thank you, sir.

Well, certainly, Mr. Chairman and Senator Cannon, it is a privilege for me to be here. I have submitted for the record as you mentioned a 51-page statement and also a 4-page executive summary. I would just like to make a few introductory remarks, if I might, and have those statements submitted for the record.

There are specific problems with the Commission's definition of deception. First, the definition is not clear, despite its 44-year history. The courts tend to give the Commission very wide latitude, and the Commission's own case law is not clear and consistent. As a result, businesses do not know what they can and cannot do. Consumers do not know what protections they do and do not have. The Commission really does not know what cases to bring and what not to bring, and the courts do not know which Commission decisions to affirm and which to reverse. As a result, they tend to defer to the agency.

Further, the Commission often wastes resources on trivial cases. For example, in the Poli-Grip case, cited in my testimony, the product is low in cost, it is frequently purchased and is easy to evaluate. Given these three characteristics, it is very unlikely that deception would take place because the maker of Poli-Grip would not be able to stay in business if it was really deceiving consumers.

Worse, the Commission often harms consumers. It tends to waste resources on the trivial, with resulting opportunity costs. Instead of wasting resources on the trivial, it could go after cases that really matter. Sometimes it engages in strained interpretations of advertisements, interpretations that ordinary consumers themselves would not make. Sometimes in its zeal to protect the unreasonable few it takes actions to the detriment of the overwhelming majority.

Let me cite a couple of examples. Before the EPA mileage tests were available, the Commission came down hard on incipient behavior by automobile companies to advertise the mileage ratings of their automobiles.

During the 1950's, the Federal Trade Commission dampened activity on the part of cigarette companies to advertise the tar and nicotine content of their products. The 1960 annual report of the FTC includes a rather remarkable sentence. It says:

> In the most important achievement under [the FTC's cigarette advertising guides'] program, the seven major manufacturers agreed to delete all tar and nicotine claims from cigarette advertising—a noteworthy example of industry/government cooperation to eliminate a practice considered deceptive and confusing to the public.

Surely at that time the data was not as good as what we have now with the testing laboratory, but by stamping out that incipient behavior to advertise and respond to consumers' interests in the tar content and nicotine content of cigarettes, I think the Federal Trade Commission injured the overwhelming majority of consumers.

Now, Senators, as you know, I have proposed that Congress define deception in the FTC Act. Under the definition I recommend, a deceptive act or practice would consist of a "material representation that is likely to mislead consumers, acting reasonably in the circumstances, to their detriment; or a material representation that the representor knew or should have known would be misleading."

I think adopting such a definition, by providing legislative standards, would focus the Commission's resources away from trivial cases and toward cases that really do matter to consumers. It would restrain the Commission from harming consumers as well. The definition, in addition, would protect vulnerable groups.

I think it is a workable standard. It tracks common law. It contains the reasonable-person standard that is well known in common law, the materiality element that is well known in common law, and the negligence standard that also is well known in common law.

It also tracks the Commission's 1975 policy protocol with respect to advertising. The questions in that protocol go to the definition I have recommended, and arguably, the Commission has been following this protocol although it may not have observed it in all cases.

Thus, I do not think there would be excessive litigation in the establishment of the parameters of the new definition. Nor would this definition restrain the Commission from bringing cases easily, when it seeks to bring the kinds of cases that really do matter to consumers.

Now Senators, I think you see sitting here in this chair an anomaly—the head of a regulatory agency asking Congress for more guidance, and that is not often heard, at least not in my research about regulatory agencies. But I believe very firmly, sir, in our constitutional form of government and I have sworn to uphold it.

Three days ago I had the privilege on the west steps of the Capitol to hear President Reagan say, "our Constitution was not written to protect the Government from its people, it was written to protect the people from their Government. James Madison said in the Federalist Papers:

> If men were angels, no government would be necessary. If angels were to govern men, neither external nor internal controls on government would be necessary. In forming a government which is to be administered by men over men, the great diffi-

> culty lies in this: you must first enable the government to control the governed, and in the next place, oblige it to control itself.

Now, our Founding Fathers vested with Congress, I believe, both the right and the responsibility to establish laws. As you, Senator Packwood, said in a Senate speech in October of 1972:

> It is incredible that the Members of Congress who have spent the better part of their adult lives asking the voters of their respective constituencies to delegate to them the power to determine the policies of this country should now run from the chance to make those decisions.

I think that sentiment is shared by many of your colleagues. I was reading last night the debate that took place on the 1980 Improvements Act. Senator Cannon mentioned that he was concerned about the tendency of the Federal Trade Commission to go beyond its statutory authority or what Congress originally intended.

I have heard Senator Kasten and Senator Ford say very similar things. I feel very strongly, sir, that it should be Congress that makes those decisions, not five unelected officials.

In conclusion, I hope the committee recognizes my themes; I believe we should reduce the uncertainty attendant with the present broad discretion given to the Commission. I believe that people have a right to know what this Government expects of them. Businessmen and businesswomen have the right to know what is and is not permissible behavior. Consumers have a right to know what kinds of protections the Government does and does not provide.

I believe that Government agencies, including the FTC, should be held accountable for their actions. Businessmen, consumers, and Congress should be able to judge the fairness and effectiveness of FTC enforcement, and the agency should know by what yardstick it will be held accountable.

I believe that insofar as possible, we should have a government of rules, not of people. Laws should be made by Congress, not by bureaucrats.

Mr. Chairman and members of the committee, there is an old saying: You cannot fix the roof when it is raining, and when the sun is shining, there is no need to fix it. I hope this does not pertain in this situation, and I ask that Congress please fix the roof before it rains.

Mr. Chairman and members of the committee, that completes my remarks. I would be glad to respond to any questions you might have.

The CHAIRMAN. Your quote from my speech illustrates the danger of having my ex-staffers work for you. I think she wrote that speech.

Mr. MILLER. That is good material.

The CHAIRMAN. Let me ask you this. What you are asking for is a legislative standard rather than an ad hoc Commission-administered standard that can jump back and forth as the Commission changes.

Mr. MILLER. That is right.

The CHAIRMAN. But I also sense that you are not asking for a broad statutory standard that allowed you to bring all kinds of actions against advertisers. You are looking for a narrow standard.

Mr. MILLER. Well, sir, I would make a distinction between unbridled discretion and limited discretion. There should be enough discretion for us to take the kinds of cases that matter, but there should not be such broad discretion that we could be meddlesome or that we could waste the Commission's resources on things that do not matter.

The CHAIRMAN. I think what all of us are frustrated by, Jim, is this. There are ads that are deliberately deceptive. You know it, I know it. They are a minority, but there are cheats in business just like there are cheats in Congress and cheats everyplace else. You try to find a way to support and actually protect the public against the occasional unknown harms that in their good judgment they cannot protect themselves against.

So let me ask you the first question, because I did read your entire statement, although I will say that your aide said, oh, it is about a 30-page statement, which was false and deceptive.

Mr. MILLER. Yes, sir.

The CHAIRMAN. I read the entire statement. As a rule of thumb, would you say that if a product does not cost very much, the Poly-Grip example, and the consumer could easily move from one product to another, that is probably not something that the Commission should waste its time on, even where the ads are clearly false?

Mr. MILLER. Well, if the market is very competitive, it is unlikely that deception would occur because it would not be a successful business strategy. Poli-Grip's maker simply would not stay in business if it really did deceive consumers. On the other hand, if you found that even though the product was fairly low in cost but a lot of consumers were deceived, the total injury could really mount up and it would be something the Commission should go after and look into.

The CHAIRMAN. If you had the situation of the ad that says "our tires stop 25 percent faster than our competitor's tires," when indeed they do not, or indeed what "25 percent" means is unclear, under your standard what can the Commission do?

Mr. MILLER. The Commission could take issue with that. Obviously, if a test showed that the actual number was 23 or 27, we might quibble about the margin. But we would ask that company to substantiate its claim, and under our standard, if they could not substantiate that claim, it could very easily and quickly be taken off the air and out of whatever medium it is in.

The CHAIRMAN. Howard, I have just received the call from the Finance Committee, and I have to go. I will be back I hope in about 15 or 20 minutes.

Excuse me, Mr. Chairman.

Mr. MILLER. Yes, sir.

Senator CANNON [presiding]. If someone makes a false claim concerning a product that costs 88 cents, the individual consumer has little economic injury; but assume that due to the false claim these products are sold to millions of consumers as a first purchase and competitors are substantially harmed by loss of sales. Should the FTC have authority to police this action?

Mr. MILLER. Surely. I think it should. Under the standard I have recommended, there would be consumer injury, and we could take issue with such a case.

Senator CANNON. With the courts taking a hard look at agency action, independent agency action is subject to closer scrutiny than in the past. The Commission may have relied on solely its own expertise in the past, but tougher standards of judicial review will require the Commission to have more evidence to back up any action taken. Does this tougher scrutiny answer many of your criticisms concerning past judicial deference to Commission expertise?

Mr. MILLER. Senator, it might and it might not. It is hard to say. If you look at the evidence, the courts have been less lenient with the FTC than in the past, especially in the antitrust area. We do not notice as substantial an increase in the courts' surveillance of the FTC's actions in the consumer protection area, but we cannot be certain.

One thing that to me is appealing about a statutory standard such as this is it would clarify what the Commission's authority is as well as what it is not. The courts conceivably could go much further and even restrain the Commission from being able to look into cases that really did deceive and mislead consumers.

So it is really hard to predict whether the courts' increasing surveillance is a trend that will continue and, if so, whether it might not turn the other way, and just what form such increasing surveillance would take.

Senator CANNON. How does your proposal affect the Commission's authority over statements that are deceptive by omission?

Mr. MILLER. Well, it would allow the Commission to pursue appropriate cases. In the standard I have recommended, deception would be a material representation that the company knew or should have known would be misleading. We could go after such cases because in certain instances the omission of an item would convey false information.

Reasonable consumers expected certain attributes of a product; for example, if you advertised an automobile that didn't come with tires, it would be false and misleading if the advertiser didn't disclose that.

Senator CANNON. How should the Commission evaluate an advertisement targeted at all consumers but relevant to a vulnerable group as well?

Mr. MILLER. Well, in such cases we have to make a determination on whether the benefits to the overwhelming majority would substantially outweigh the cost to the vulnerable few. We have to look very carefully at vulnerable groups. For example, the elderly might be easily misled by an advertisement that someone has a miracle cure for cancer, or there may be an advertisement that is directed toward a majority of consumers which may inadvertently affect a small vulnerable group, like advertisements showing a child riding a tricycle out in the street. We could go after that, under the second provision of the standard, the provision that says that the representer knew or should have known that it would be false or misleading. We could also, I think, go after it under the reasonableness-plus-consumer injury test, because what is reasonable depends on the circumstances.

Senator CANNON. What effect would your proposal have on deceptive practices other than advertising challenged by the Commission?

Mr. MILLER. Just as in the advertising area it would cause us to channel our resources more toward those things that really matter to consumers where there would be consumer injury. In certain cases we could simply rely on the second provision; that is, when there was a material representation that the representor knew or should have known would be false on misleading.

So I think that in terms of our practices, whether it be high pressure sales tactics or whatever, that the kind of standard that I have recommended would allow the Commission to go after those kinds of cases that really matter but not squander its resources and not go after cases that might harm consumers.

Senator CANNON. Thank you very much, Chairman Miller. We appreciate your being here and giving us your views this morning.

Mr. MILLER. Thank you, sir.

[The statement follows:]

STATEMENT OF HON. JAMES C. MILLER III, CHAIRMAN, FEDERAL TRADE COMMISSION

Mr. Chairman and Members of the Subcommittee: I am very pleased to be here today to discuss with you proposals to amend the Federal Trade Commission Act by defining the term, "deceptive acts or practices" as it appears in Section 5 of that Act.

The goal of the Commission, now as in the past, is to foster a competitive marketplace free of unfairness and deception. To accomplish that goal, I believe it is vital for the Commission to receive explicit legislative guidance.

Mr. Chairman and Members of the Subcommittee, I should note that the views I express here today do not necessarily reflect the views of the other Commissioners. As you know, my colleagues on the Commission oppose defining the term "deceptive acts or practices" at this time, although Commissioner Clanton agrees that the subject is worthy of serious examination, possible leading to recommendations for legislative action at some future date.

In the remainder of these introductory remarks, please let me address the major issues that give rise to my opinion that a statutory definition of deception is needed.

Section 5 of the Federal Trade Commission Act prohibits "unfair or deceptive acts or practices." To date, the determination of whether a marketing, selling, or advertising practice is deceptive has been left entirely to the discretion of the Commission, since there are no statutory standards. As Professor Rosden has written in his treatise, The Law of Advertising:

"It has been said sometimes, and not without a measure of truth, that an advertisement is deceptive if the Federal Trade Commission calls it so. This situation, unusual as it is in American jurisprudence, is due to a combination of reasons. In the first place, Congress has not seen fit to set legislative standards that have an ascertainable degree of definiteness. Nor has Congress written standards into the Act after several decades of administrative and judicial ad hoc interpretations."[1]

The absence of standards under which the Commission has pursued cases of deception has frequently resulted in Commission actions that have done consumers more harm than good. For example, the Commission has prohibited acts and practices that could benefit the majority of consumers simply because those acts and practices also has the tendency to mislead an unreasonable few. This problem is particularly prevalent in cases—discussed more fully below—in which the Commission has brought enforcement actions against advertisers for claims that reasonable consumers would not believe the advertisement made. These incluse clearly subjective claims, "puffing", and opinions which were accurately reported.

The Commission also has challenged alleged deceptive acts and practices that are not likely to cause consumers any injury. In these cases, the Commission's scarce enforcement resources have been squandered on the trivial. Examples of this—again, discussed below—are Commission cases challenging discount pricing claims and claims concerning products that are low in price, are frequently purchased, and are easy to evaluate.

I believe that the best, certainly the most lasting, solution to these problems lies with Congress. What is needed, I submit, is for Congress to provide a statutory definition of deception.

The definition I respectfully recommend for your consideration is as follows: A deceptive act or practice is a material representation that: (a) Is likely to mislead consumers, acting reasonably in the circumstances, to their detriment; or (b) The representor knew or should have known would be misleading.

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[1] Rosden, The Law of Advertising, § 18.03, at 46–47 (Volume 2, 1976; notes omitted).

Under this recommended definition, an act or practice would violate Section 5 if consumers acting reasonably would likely be mislead to their detriment by a material representation, or if the one responsible for the act or practice knew or should have known that a representation relevant to the selling point was misleading. Under the "knew or should have known" standard, the Commission would not be required to show a likelihood of consumer injury.

This testimony explains why defining deception by statute is necessary and will advance the public interest, benefitting both consumers and businesses. The policy, rationale, and implementation of the first part of the recommended definition—that pertaining to the likelihood of injury to consumers acting reasonably in the circumstances—are addressed in the next section. Then, I discuss how the other part of the definition allows for prosecution of deceptive acts and practices without having to demonstrate a likelihood of consumer injury and why enforcement under this provision in certain situations would be sound public policy. Finally, I explain why it would be preferable for Congress to legislate these standards, even though they could be adopted by the Commission on its own volation.

MATERIAL REPRESENTATIONS THAT MISLEAD CONSUMERS, ACTING REASONABLY IN THE CIRCUMSTANCES, TO THEIR DETRIMENT

As described below, the reasonableness provision incorporated in the recommended definition is sound public policy, protects the interests of consumers in the free flow of truthful information, and ensures that the Commission's scarce resources are not squandered on cases in which few consumers are likely to be misled. Because the reasonableness provision would consider the circumstances—such as the intelligence, sensibilities, and experience of consumers that might be affected by the advertising message—the provision would also protect children, the aged, the infirm, and other groups that might be particularly vulnerable.

Also set forth below is the rationale for the part of the provision having to do with "detriment", or consumer injury. In brief, I believe that the Commission should challenge only those acts or practices that are likely to reduce consumer welfare. The Commission's responsibilities in policing the American marketplace are too vast and its resources too modest for it to pursue acts and practices unlikely to injure consumers.

As with reasonableness, statutory codification of a provision requiring the Commission to find that the challenged practice is likely to result in consumer injury would not impose unreasonable evidentiary burdens on the Commission. In many cases, the proposed changes would still allow for an inference that a representation results in consumer injury. Moreover, a requirement that the Commission in fact prove the likelihood of injury before it challenges an advertising claim or a marketing practice is not a requirement for extensive analysis or sophisticated econometric evidence.

Equally important, the definition I recommend is a workable one. It would of course eliminate some cases the Commission might have pursued, as it should. But in cases where Commission action is clearly appropriate, the recommended definition would impose no greater burden on the agency than at present.

CONSUMERS ACTING REASONABLY IN THE CIRCUMSTANCES

At common law, a claim that a representation is deceptive would hinge on "reasonable" interpretations of it. The significance of the seller's words are determined according to the effect they produce, under the circumstances, upon the ordinary mind.[2] In my opinion, the common law notion of "reasonableness" provides a framework for sensible Commission enforcement against deceptive marketing, selling, and advertising practices. Two problems exist with challenging truthful representations that reasonable or ordinary consumers understand correctly. First, such cases misuse the FTC's resources. When few consumers misunderstand the representations, few can be injured. Second, cases against claims misunderstood at most by only a small minority injure the majority of consumers. By prohibiting such representations, the Commission makes it more difficult for consumers to receive truthful and useful information about goods and services they might purchase.

Communication with consumers is a difficult task even without unnecessary obstacles imposed by the Commission. In many instances, firms may not have adequate market incentives to provide information. Since it is costly to generate and disseminate information, anything that imposes a barrier to communication, such as a government regulation, may further dry up useful information. Even when firms provide information, they often find it difficult to attract and hold consumers' attention long enough to communicate the intended message effectively. And, for consumers, locating and processing information are costly activities. When firms have overcome these obstacles and have been able to provide useful information to a large audience of reasonable consumers, we should be careful not to intervene just because a small minority of consumers acting unreasonably might be misled.[3]

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[2] See W. Prosser, Law of Torts (4th ed.; 1971).

Furthermore, by impairing the efficient operation of the advertising market, such over-zealous enforcement might ultimately compound this harm to consumers by reducing competition among sellers of goods and services. The marketplace operates more vigorously and more responsively when consumers are aware of alternative sellers, products, and prices. To the extent information concerning these choices becomes more costly to obtain, less information will be produced and disseminated, and consumer awareness about potential choices will be diminished.[4] The result is a less competitive marketplace, with higher prices and fewer real choices.

IMPROPER PROSECUTION DUE TO STRAINED INTERPRETATIONS

Consumers are hurt when the Commission restricts the dissemination of information useful to them.[5] When information that may mislead some, but not the overwhelming majority is prohibited, the majority, goes without information that could be very useful. This problem is particularly prevalent in cases in which the Commission improperly interprets the meaning of an advertisement.

Over time, the courts have deferred to the Commission's presumed expertise in determining the meaning of an advertisement. Ira Millstein, a well-known trade regulation lawyer, has stated:

"The Federal Trade Commissioners themselves are not chosen for their expertise in ascertaining the meaning of advertisements, or for some general intuitive knowledge to the public's understanding of sights and sounds. Of the five present Commissioners, not one has had prior experience in business, let alone advertising. Nor is such expertise invested with the robe. That the Commission's task under the statute is to act in the field of false advertising does not make the Commissioners any more capable of ascertaining the meaning of an advertisement's promise, whatever the intelligence standard selected, than any other five men (or possibly three), or reviewing court. Rather, courts should occupy in the advertising field the same appellate role thay play in reviewing other administrative determinations—no greater perhaps, but cetainly no less." [6]

Or, as former Federal Trade Commissioner Robert Pitofsky has stated: "Why questions of meaning should be submitted to the virtually unreviewable discretion of five Commissioners of the FTC has never been articulated. Unlike other instances of deference to regulators as part of the administrative process, there is no reason to believe that commissioners of the FTC have unusual capacity or experience in coping with questions of meaning, nor any indication that successful regulation of advertising requires a balance of related regulatory considerations that commissioners are in a special position to handle." [7]

The Commission's recent case in *Kroger* [8] is but one example of the tendency of the Commission to pursue interpretations of advertising claims that reasonable consumers would not believe the advertiser made. In this case the company, Kroger, described the results of its "Price Patrol," in which homemakers surveyed prices of 100 to 150 items at local supermarkets. Without any evidence of the meaning conveyed by the ad program, the Commission held that the ads implicitly represented that the surveys were "methodologically sound" and "statistically projectible." Commissioner Patricia Bailey dissented on the meaning of the ads. She noted that Kroger made a point of emphasizing the informality of the surveys. She wrote:

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[3] See Beales, Craswell and Salop, "The Efficient Regulation of Consumer Information," 4 J. L. Econ. 491 (1981). When the consequences to those who are misled are extremely severe, the costs to the minority may outweigh the benefits to the majority. The Commission can, and should act in such cases, either under the "knew or should have known" standard discussed below, or under an unfairness theory.

[4] It is the interest in the free flow of truthful information that has led to the extension of the First Amendment's protection to commercial speech in recent years. See *Central Hudson Gas & Electric Corp.* v. *Public Service Comm'n*, 447 U.S. 557 (1980); *Bates* v. *State Bar of Ariz.*, 433 U.S. 350 (1977); *Virginia State Bd. of Pharmacy* v. *Virginia Citizen Consumer Council, Inc.*, 423 U.S. 748 (1976).

[5] In addition to being deprived of product information, consumers are also deprived of their right to receive that information. As the Supreme Court has held, "[i]f there is a right to advertise, there is a reciprocal right to receive the advertising." *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 757 (1976).

[6] Millstein, "The Federal Trade Commission and False Advertising", 64 Colum. L. Rev. 439, 492–93 (1964; footnote omitted).

[7] Pitofsky, "Beyond Nader: Consumer Protection and the Regualtion of Advertising," 90 Harv. L. Rev. 661, 678 (1977).

[8] Kroger, Co., D. 9102 (Sept. 25, 1981), appeal docketed, No. 81-7937 (11th Cir. Nov. 23, 1981).

"The notion that these surveys were 'methologically sound' and therefore 'prove' an overall 'projection' of lower prices is simply, in my view, an artificial construct imposed by the majority [of the Commissioners] on the ads in question." [9]

On the merits of bringing the case, she wrote: "I fear that the majority opinion will chill the development of useful comparative pirce adertising, especially among retail grocers, which is extremely useful to the public, particularly in times of high inflation." [10]

In *Camp Chevrolet,*[11] an ad claimed "Camp Chev Wins Economy Run! Vega No. 1." The ad went on to describe truthfully the local sports car club mileage test upon which the claim was based. The ad explained that "[s]ome of the drivers were highly experienced in coaxing good gas mileage out of their cars, while others were just the average driver . . .", and that "[s]ome of the cars were prepared specially for the run. . . ." [12] The Commission, however, unreasonably interpreted the ad as implying that the *average* driver could get the same results with a Vega. The Commission ordered Camp to stop making any claims on fuel economy of any vehicle unless "the representations reflect the average consumer's customary or usual driving experience." [13] As a result, consumers were unable to read about and evaluate the truthful report on the sports club test.

In a litigated case, *Ford Motor Co.,*[14] the headline of the challenged ad claimed that "All 5 Ford Motor Co. small cars got over 26 mpg." The ads stated that mileage varies according to maintenance, equipment, total weight, driving habits, and so forth, and added that no two drivers, or even cars, are exactly alike. Despite these disclaimers, the Commission unreasonably found an implied claim that the *average* driver would get the advertised mileage, notwithstanding a survey by Ford that suggested reasonable consumers did not so interpret the ads.

Both the *Camp Chevrolet* and *Ford* cases took place *before* the Environmental Protection Agency began tests to report comparative mileage figures for automobiles. Thus, attempts by auto companies to provide relevant information to consumers were undermined by Commission action.

These cases indicate the problem created by the lack of a specific standard for deception. In each, the information prohibited or curtailed was undoubtedly useful to many consumers. It was information that could have assisted them in making their purchasing decision. To the extent that consumers were deprived of that information, those consumers were harmed by the Commission's action.

SUBJECTIVE CLAIMS, PUFFING CLAIMS, AND ACCURATELY STATED OPINION CLAIMS

In addition to the strained interpretations described in the preceding section, the Commission, in the past, has pursued a variety of subjective claims, obviously exaggerated statements, and correctly stated descriptions of opinion based upon interpretations that reasonable consumers were unlikely to hold.

Subjective claims, including those regarding taste, feel, scent, appearance, and ease of use, are important and convey useful information. They are, however, inherently difficult to measure objectively. For example, it is difficult to describe a flavor other than to explain how it tastes to the individual making the claim. Similarly, handling performance of automobiles is often a fairly subjective matter. Hence, a seller may opine, "it handles great" to inform consumers that the automobile's handling characteristics may well be a plus, and that consumers who are looking for a car with good handling characteristics might well want to test drive the advertised vehicle. The typical consumer, in other words, interprets such subjective claims as an invitation to evaluate the product, not as a claim upon which to make an irreversible commitment.

The Commission has of course stated that it does not pursue subjective claims. For instance, in *Fedders Corp.* v. *FTC,*[15] on appeal the respondent argued that an order was overly broad because, among other things, it was aimed at "subjective arguments which merchants sometimes indulge in while hawking their wares." [16] The court did not consider the argument because it noted that "[t]he Commission, in its brief, has admitted that to the extent that Fedders makes claims that are solely subjective for their product, there is no need for substantiation." [17] Yet, less than a year later, the Commission issued a consent order based on allegedly false claims that a hair creme relaxer was "gentle", "cool to the scalp" and easy to use.[18]

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[9] Id. Bailey, dissenting at 3.
[10] Id. at 2.
[11] 84 F.T.C. 648 (Oct. 7, 1974; consent order).
[12] Id. at 650.
[13] Id. at 652.
[14] 87 F.T.C. 756 (1976).
[15] 529 F.2d 1398 (2d Cir. 1976).

Likewise, obviously exaggerated or puffing statements, such as "the best money can buy" are useful also. The typical consumer readily understands that the advertisement is not to be interpreted literally. Much of advertising is signaling, conveying the message that the advertiser believes consumers will like the product.[19] The key to producing these signals is memorable advertising. If obvious exaggerations help consumers to remember the product's name, they reduce the cost of providing the signal. As a result, consumers as well as advertisers benefit. When the Commission challenges such advertising, as it has in the past, it reduces the efficiency of what is already a very expensive process.

In *Lear Siegler*,[20] a case culminating in a consent order, the Commission interpreted the claim "World's Finest Helmet" displayed on motorcycle helmet cartons as meaning that the helmets were superior in quality and safety to all other safety helments. By any objective standard of consumer interpretation, "World's finest" would be considered a "puff," yet the Commission prohibited representations with respect to the safety aspects of any product unless they are based on "competent, controlled scientific tests conducted by experts, the results of which are available for inspection by the general public." [21]

On a related matter, the utility of *correctly stated* opinions should be obvious. Accurate reports of opinions give consumers access to the conclusions of theose more knowledgeable at low cost.[22] For example, it may be useful for consumers to know that the Surgeon General has concluded that cigarette smoking is hazardous; or that the American Heart Association has determined that it is prudent to reduce fats and cholesterol in the diet; or that Road and Track magazine believes that the Vega is the best handling passenger car ever built in the U.S.[23]

WORKABILITY OF REASONABLENESS STANDARD

Although for the reasons outlined above, a reasonableness standard for deception is sound policy, to be useful it must be sufficiently workable to allow the Commission to continue vigorous prosecution of truly deceptive marketing, selling, and advertising practices. I believe that such a standard is workable and is unlikely to increase the Commission's evidentiary burden.

In many instances, the meaning of a representation to the typical consumer is likely to be apparent on the ad's face. An ad that claims "our product will prevent colds" is going to mean exactly that to most reasonable consumers. Similarly, consider the ad that claims "our product will kill bacteria. Take it when you feel your next cold coming on." Such an ad is likely to lead most reasonable consumers to believe both that bacteria are a significant cause of colds and that the product will prevent colds.

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[16] Id. at 1404.

[17] Id. 1404, n.6.

[18] Johnson Product Co., 87 F.T.C. 206, remanded 549 F.2d 35 (7th Cir. 1977), reissued 91 F.T.C. 506 (1978). In my opinion, failure to disclose health hazards associated with the product may have otherwise justified the consent order.

[19] See Nelson, "Information and Consumer Behavior," 78 J. Pol. Econ. 311 (1970).

[20] 83 F.T.C. 503 (1973; consent order).

[21] Id. at 506.

[22] This, of course, does not permit unscrupulous advertisers to dress up misleading statements in the guise of opinion, as some critics charge. A representation of an opinion is a factual claim that the person or institution holds the advertised opinion. Misrepresentations of opinions are clearly subject to challenge. Similarly, it is quite possible to misrepresent the degree of expertise of the source of an opinion. See, e.g., Leroy Gordon Cooper, 94 F.T.C. 674(1979) (By endorsing an automotive product, Cooper, an astronaut, represented that he was a trained and knowledgeable expert in automotive engineering).

[23] General Motors Corp., 85 F.T.C. 17(1975). In this case, General Motors advertised that Road and Track magazine found the Vega to be the best handling passenger car ever built in the U.S. The Commission interpreted the claim to mean that GM was alleging proof that Vega is the best handling car and found that Road and Track magazine was not adequate substantiation for that claim. As a result consumers were deprived of valuable opinion information from a reputable publication.

At common law, the meaning of a communication is a question of fact for the jury when statements are capable of multiple interpretations. The jury is asked to assess the meaning of the statements to a reasonable person under the circumstances. With a reasonableness standard for deception in FTC law, the Commission would be asked to base its interpretations on facts demonstrating how the ordinary consumer would interpret the challenged representation. In many cases, the representation itself may be the only evidence necessary. Only when it is difficult to predict how typical consumers interpret an ad will it be necessary to test those predictions with extrinsic evidence. The alternative is to decide factual questions based on introspection rather than on evidence, a practice that has led to the problems discussed above.[24]

Recent cases where advertising did misled consumers acting reasonably in the circumstances to their detriment could have been prosecuted easily under the reasonableness standard. In *Sears, Roebuck*,[25] the Commission interpreted the claims for Lady Kenmore dishwashers as would reasonable consumers. For instance, the ads claimed:

No scraping. No pre-rinsing.

It gives you freedom from scraping and prerinsing because it has two hot water jets to scour soft food off dishes, and a built-in stainless-steel pulverizer that grinds up leftover food.

With a Kenmore you'll never have to scrape or rise again. Even dishes crusty with leftover food. Kenmore's 14 powerful hot water jets scour every dish clean . . . with no scraping or rinsing.[26]

The FTC's administrative law judge granted partial summary judgment regarding the meaning of this and other claims. In arguing the case before the Commission, Sears did not challenge the ALJ's finding that it represented that Lady Kenmore would eliminate the need for pre-rinsing and scraping. Nor do I see how it could have done so under the reasonable interpretation standard I recommend. There is simply no other way for a reasonable person to have interpreted Sears' claims.

Similarly, In *Fedders Corp.*,[27] the respondent's room air conditioner advertisements stated:

"Reserve Cooling Power—only Fedders has this important feature. It's your assurance of cooling on extra hot, extra humid days.

"Reserve Cooling Power—it's Fedders engineering "extra" which gives maximum cooling even when sunload reaches 115 degrees—and other units fail."[28]

The Commission's complaint alleged that the respondent misrepresented that its air conditioner contained a performance feature not found in competing products. The meaning that the ordinary consumer would reach was clear from the face of the advertisements. In fact, the respondent did not even challenge complaint counsel's interpretation.

The Listerine mouthwash case is another example in which the Commission gave advertising claims a reasonable interpretation and in which proof would have been no more difficult under the standard I recommend. In that case, the ALJ and the Commission found that the company made claims that Listerine will ameliorate, prevent, and cure colds and sore throats. Some of the claims were:

"Listerine Antiseptic Kills Germs by Millions on Contact. For Bad Breath, Colds and Resultant Sore Throats.

"Fight back with Listerine Antiseptic. Gargle twice a day—starting now—before you get a cold. You may find the colds you do get will be milder; less severe. That's why more people use Listerine during the colds—catching season than any other oral antiseptic."[29]

Unlike *Sears* and *Fedders*, testimony was presented in this case on consumer interpretation of the ads. The ALJ considered expert testimony from both sides on the meaning of the ads with respect to claims that Listerine would prevent and cure the common cold. Obviously, a requirement that the meaning of the ads to reasonable consumers be established could not have complicated that particular proceeding.

Indeed, contrary to what some critics contend, even when the respondent submits evidence challenging the complaint counsel's interpretation of an advertisement, the reasonableness standard I have recommended need not create a significant burden on the staff in appropriate cases. *Chrysler Corp.* illustrates this proposition.[30] One of the advertisements was entitled "The Small Car versus the Small Car." The text under this caption stated:

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[24] For example, it would have been appropriate to require staff to demonstrate with evidence that reasonable consumers reached the interpretation alleged by the Commission in the Ford mileage and the Kroger Price patrol cases.

[25] Sears, Roebuck & Co., 95 F.T.C. 406 (1980), aff'd, No. 80-7368 (9th Cir. May 6, 1982).

[26] Id. at 406-19.

[27] 85 F.T.C. 38, (1975), aff'd, 529 F. 2d 1398 (2d Cir. 1976).

[28] Id. at 39, 54.

[29] Warner-Lambert Co., 86 F.T.C. 1398 (1975), aff'd as modified, 562 F. 2d 749 (D.C. Cir. 1977), cert. denied, 435 U.S. 950 (1978).

"You can buy a Chevrolet Nova *or* you can buy a small car that can beat it on gas mileage. * * *

"The answer is a small car at your Chrysler-Plymouth and Dodge Dealer's

"See all the Darts at your Dodge/Dodge Trucks Dealers."

Pictured in the advertisement were a Dodge Dart Swinger and a Plymouth Valiant. The asterisks in the text were keyed to the following footnote:

"Gas mileage figures based on October 1973 Popular Science magazine. Test performed by Popular Science for its report were conducted on 1973 vehicles with figures adjusted by Popular Science for 1974 model changes and the results of E.P.A. tests."

The Popular Science tests showed that Valiants and Darts equipped with six-cylinder engines got better gas mileage than Chevrolet Novas with either a six or eight-cylinder engine. However, the tests also showed that Valiants and Darts with eight-cylinder engines got poorer gas mileage than Novas with six or eight-cylinder engines. The staff interpreted the challenged ads as conveying the representation that Popular Science had reported that all Valiants and Darts were superior in mileage to all Novas. Chrysler challenged this interpretation and submitted a "focus group" study to show that the consumers perceived "small cars" as those with six-cylinder engines and smaller. The Commission found the study's deficiencies substantial and its probativeness on the issue of the ads' meaning slight.[31] The Commission in fact applied a reasonableness standard in its evaluation of the ad:

"The ads refer broadly to Chrysler 'small cars' and invite consumers to see 'all the Darts' and 'the Dusters and Valiants,' without any stated references to cars, engines. It would not be readily apparent to consumers from any information the ads contain that the mileage claims were limited to small cars with six cylinder engines; nor are the references to Popular Science qualified in any way which would assist consumers to understand that the magazine's support for Chrysler's fuel-economy claim was confined to six-cylinder cars. Thus, viewed in their entirety, we believe the ads would reasonably lead consumers to believe that the mileage claims referred to six and eight-cylinder cars and to vehicles equipped with comparable-sized engines."[32]

In sum, requiring the Commission to interpret representations as would a reasonable consumer is a practical standard. It allows the Commission to pursue appropriate cases of deception with undiminished vigor.

PROTECTION OF VULNERABLE GROUPS

Some groups in the population need protection more than others. Children, the elderly, and people with serious illnesses are clear examples. But protection of these groups is fully consistent with the reasonable interpretation standard I recommend. What is reasonable is not absolute; instead, reasonableness depends on the circumstances, including the age and sophistication of the ad's audience. Camera angles and photographic techniques that may exaggerate the size or speed of a toy, for example, may mislead the typical child, but not the typical adult. Similarly, an advertisement that is only relevant to a particular group is to be evaluated against the reasonableness of that group. A product that claims to be a miracle cure for terminal cancer victims is not likely to have substantial appeal to other groups, and should be judged against the standards of reasonable interpretation given that the audience is terminally ill. In such a case, there is no policy reason to protect the interests of nonvulnerable consumers because they have no interest in what the advertiser wishes to convey. The members of the targeted groups, however, do have an interest in truthful, useful information aobut products of particular relevance to them.

Thus, for example, the reasonableness standard would have allowed the Commission to challenge the deceptive advertisements and practices directed at the seriously ill in Travel King, Inc.[33] In this case, the ALJ discussed the advertisements and promotion of a tour to visit "psychic surgeons" who allegedly cured various illnesses with painless "surgery" that was really sleight-of-hand trickery. Although the ordinary person without health problems would be likely to reject these incredible healing claims as unreasonable, the Commission properly considered the desperate condition of the specific audience to whom the ad was directed. Recognizing the vulnerability of the audience, the ALJ found that:

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[30] 87 F.T.C. 719 (1976), aff'd as modified, 561 F. 2d 357 (6th Cir. 1977).

[31] 87 F.T.C. at 747-50.

[32] 87 F.T.C. at 746-47 (notes omitted).

[33] 86 F.T.C. 715 (1975).

"[m] any thousands of ill persons from all over the world seem to have made the trip, drawn by the desperate but futile hope that by some magic their bodies will be opened by Phillipine 'healers', and the causes of their diseases removed." [34]

The ALJ also found that the respondents' practices: "inflict great injury and suffering on persons afflicted with serious incurable or terminal illnesses and diseases, to prey upon and to exploit them, and to cause them, . . . to undertake long journeys at great costs, hardship and inconvenience, and to forego medical treatment with the potential result of worsening their condition and hastening or causing their death." [35]

The Commission adopted the ALJ's findings of fact, including a determination that a disclaimer would not remedy the deception. In doing so, it states:

"Because we are dealing here with desperate consumers with illnesses who want to believe that 'psychic surgery' will cure them, no amount of disclosure will suffice to drive home to all the point that 'psychic surgery' is nothing but a total hoax." [36]

Because the reasonable interpretation approach focuses on the perceptions of the target audience, it certainly provides no less protection for vulnerable groups than does the current unbounded law and may well provide more. Protection of vulnerable groups is lifted from the realm of agency discretion into a principled policy engrafted in the statute.

REQUIREMENT FOR CONSUMER INJURY

Under common law, a finding of injury is implied in the requirement for materiality. This principle of common law as applied here has two elements. First the consumer must rely on the claims; second, the consumer must rely on the claim to his or her detriment.[37] That the Commission's statutory mandate contain such an element simply makes good sense. The Commission's responsibilities in policing the American marketplace are too vast and its resources too modest for it to pursue misrepresentations when injury is unlikely.

A legal doctrine that allows such cases substitutes the Commission's instinct about what is wrong for the market experience of consumers as a guide to when government intervention is warranted. In a society in which commercial speech is protected by the Constitution, it is anomolous to me that the FTC has power to interfere with advertising without demonstrating any countervailing injury to consumers.

To determine if consumer injury is likely, the key question is whether consumers have given up something of value by their reliance on the misleading claim. Consumers will not give up anything of value unless the product is worth more to them if the claim is true than false. For example, when an advertiser claims that a product has a certain feature that consumers would like, we can normally assume that the product is worth more to consumers if the claim is true. Thus, if a dishwasher manufacturer has survey evidence indicating that consumers prefer to avoid the need to rinse dishes first, that would constitute evidence that consumers would find a dishwasher with a no-rinse feature worth more than one without it. If there is no other evidence of likely injury, this inference that the product is worth more to consumers is sufficient to justify a finding of injury. The finding of consumer injury would be irresistable with evidence that consumers must pay more for products with the advertised feature. In the dishwasher case, for example, evidence that the price of the no-rinse dishwashers is higher than the price of ordinary ones would end debate over the injury issue.

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[34] Id. at 760.

[35] Id. at 764 (emphasis added).

[36] Id. at 774.

[37] Althouth the courts have paid lip service to the need FTC to find a misrepresentation material, in fact, the courts have permitted the Commission frequently to devote little or no attention to the issue of the importance of the challenged misrepresentation to the purchasing decision. See *FTC* v. *Colgate-Palmolive,* 380 U.S. 374, 392 (1965); In *FTC* v. *Mary Carter Paint Co.,* 382 U.S. 46 (1965), the Commission did not even explain why it believed the claim was material, but was upheld nonetheless. Moreover, proof of likelihood of injury is not necessary to a Section 5 action under the current statute. In Firestone Tire and Rubber Co., 81 F.T.C. 398 (1972), aff'd, 481 F. 2d 246 (6th Cir. 1973), cert, denied, 44 U.S. 1112 (1973), for example, the Commission stated: "Respondent argues that complaint counsel was required to show that respondent's advertisement would have been likely to cause consumers to buy its product when they otherwise would not have done so. *Bockenstette* v. *FTC,* 134 F. 2d 369, 371 (10th Cir. 1943; *Indiana Quartered Oak Co.* v. FTC, 26 F. 2d 340, 342 (2d Cir. 1928). We do not agree that these cases stand for the proposition that such a showing is required to prove deception. . . . The fact that consumers were not harmed because they would have purchased the products anyway under truthful advertisements is not relevant to this proceeding." 81 F.T.C. at 451 (notes omitted).

Even when the price of the product with the deceptively advertised feature is the same as those products without the feature, however, injury may occur. In some cases, consumers give up the opportunity to purchase another brand that actually provides the advertised feature. In other instances, consumers may have preferred to spend their money on some other product if they knew that the advertised feature was not actually available. There is injury in such cases, because consumers give up a valuable alternative by purchasing the deceptively advertised product.

Such injury is particularly likely with discretionary purchase items. For example, in today's economy the purchase of a vacation tour package is usually viewed as a discretionary expenditure. If a tour promoter deceptively lures a substantial number of consumers into purchasing its vacation package who otherwise would not have purchased a vacation tour, the consumer injury may be great. This is true even if the offending tour promoter's package costs no more and delivers as much as the vacation package offered by its competitors who did not make the false feature claims. Except for the deception, many of the purchasers would have used the funds which they spent on the offending tour promoter's vacation package to purchase a vacation that actually provided the features or to purchase alternative products, which they would have valued more highly (e.g., child's education, new car, or home improvements).

What consumers must forego if the claim is false is not necessarily money, nor need it be reduced to monetary terms. Injury exists if consumers forego some other opportunity, valuable in itself, by reason of the deception. Thus, if deceptive advertising induces consumers to drive unnecessarily across town on a Saturday, there could be significant injury in foregone leisure time from the false claim, even if the deception were cured before purchase (as is sometimes the case with bait and switch advertising).

There are many examples where the Commission has properly pursued cases where substantial injury has resulted from the foregone opportunities caused by the deception. These costs have been easy to identify even when they are not easily expressed in monetary terms. In *Travel King, Inc.*,[38] for example, respondents had advertised and promoted tours to visit "Psychic Surgeons" who were said to have cured their patients of a variety of serious illnesses. The injury was related to much more than the ticket price of the tour package because the representation caused people to go without needed medical care, thereby adversely affecting their health.

This potential for injury caused by the forebearance of proper medical care also is exemplified in a series of consent orders prohibiting the misrepresentation of acne cures.[39] An order prohibiting the misrepresentation of the efficacy of vaginal contraceptives also illustrates that non-monetary injury can result from deceptive advertising; [40] in this case, the injury is greater risk of an unwanted pregnancy.

A focus on the likelihood of consumer injury provides a useful standard for sensible enforcement policy. It would lead the Commission to avoid certain cases. One class of cases I believe the Commission should shy away from, and which the standard I recommend would restrain, involves claims that an advertised price represents a special sale price, or a substantial discount from the "regular" price.[41] The deception involves not the price at which the product is actually sold, which should be the basis for a determination of injury. Rather, the alleged misrepresentations involve the "regular" price, so that the "savings" are misstated.

It is very difficult to see why consumers would pay more for the product even if the "regular" price claim were true.[42] As former Commissioner Pitofsky wrote in criticizing the Commission for bringing such cases, "[A]s long as consumers are accurately informed of the offering price, they can make sensible decisions, and the transactions may still be at prices lower than could be obtained at most other outlets in the marketing area." [43]

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[38] 86 F.T.C. 715 (1975). See supra text accompanying notes 33-36.

[39] AHC Pharmacal, Inc. 95 F.T.C. 528 (1980); San-Mar Laboratories, Inc., 95 F.T.C. 236 (1980); Harvey Glass, M.D., 95 F.T.C. 246 (1980); National Media Group, Inc., 94 F.T.C. 1096 (1979); Karr Preventative Medical Products, Inc., 94 F.T.C. 1080 (1979); Cooga Mooga, Inc., 92 F.T.C. 310 (1978).

[40] Jordan-Simner, Inc., 95 F.T.C. 871 (1980; consent order).

[41] See, e.g., Levitz Furniture Corp., 88 F.T.C. 263 (1976; consent order).

[42] In some instances, consumers may use price as an indication of quality. If so, then misrepresenting the regular price misrepresents the quality of the goods, causing injury. What is relevant, however, is the regular market price of the product, not the regular price of this seller. With a well-known discounter, such as Levitz, the pricing claims are unlikely to misrepresent quality.

Commissioner Pitofsky further noted that these cases were most frequently brought against discounters, who were attempting to use price as a competitive weapon. Thus, not only did action by the Commission in these cases fail to help consumers, it probably injured them.

Another class of cases the Commission would avoid under my recommended standard is those in which consumers can evaluate the claim for themselves at low cost. Where these conditions are met, consumers are unlikely to forego anything of value if the claim is false. More important, it is extremely unlikely that there would be any deception in such cases. When a product is low in price, is frequently purchased, and is easy to evaluate, there is no incentive to mislead.[44] Although consumers may purchase the product once, they will not do so again. Thus, the returns from a single purchase are unlikely to cover the costs of disseminating the false advertising for a product that meets these conditions. In short, in this class of cases, the market works—deception is not a viable business strategy.

During the last few years, the FTC staff, in selecting cases, has used correctly the presence of these three conditions (low price, frequency of purchase, and ease of evaluation) as reasons for not expending valuable resources in pursuing cases. In these cases, consumers are more likely to evaluate the claim accurately than is the Commission. In fact, if there is true deception, the market place is likely to eliminate it before it comes to the Commission's attention. The statutory standard I recommend would have the effect of writing onto law the staff's case selection criteria.

From time to time the Commission's opinions have reflected this standard. Thus, in the Dry Ban case brought several years ago,[45] the Commission challenged claims that the product was dry. The compaint alleged that these claims were absolute, meaning that the product was literally dry when it was placed on the skin. The Commission ultimately dismissed the case, in part because the product was inexpensive, frequently purchased, and easy for consumers to evaluate on their own.

Other cases have slipped through, however. A recent example is the case against Block Drug for its advertising of Poli-Grip.[46] These ads claimed that the product would eliminate discomfort and embarrassment when denture wearers ate "problem" foods such as apples. As Commissioner Thompson noted in dissenting from the issuance of the complaint, the product is cheap, is purchased frequently, and the claims are easy to evaluate. As he stated:

[I]t is inconceivable to me that any denture wearer who applied Poli-Grip or Super Poli-Grip and bit into a red apple then saw his dentures smiling back at him would ever purchase the Gripper again." [47]

In other recent cases in which Commission action was entirely appropriate and justified, the need to establish the likelihood of consumer injury would not have significantly complicated the litigation. For example as noted above, in Sears,[48] the company claimed that its dishwasher eliminated the need for scraping and prerinsing. Because these are time-consuming, undesirable activities, it is reasonable to infer that consumers would be willing to pay more if the claims were true than if they were false.

Moreover, in that case, evidence of injury did exist. A market survey conducted by Sears indicated that a large segment of the public wanted a dishwaher that eliminated the need for pre-scraping and pre-rinsing, and was willing to pay more for this feature. The ability of a dishwasher to clean dishes on the upper rack was also an important factor to the public, as was the ability of a dishwasher to clean pots and pans.[49] Thus, had the claims been true, consumers apparently would have been willing to pay a premium for the product. Finally, the consumer clearly cannot evaluate cleaning performance claims without incurring a large expenditure.

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[43] Pitofsky, supra note 7, at 688.

[44] For most such products, what consumers give up is the opportunity to use a different brand of the product. In the Poli-Grip case, discussed below, most denture wearers probably use some denture adhesive anyway. Thus, any injury is the difference in product value, not the price of the advertised brand.

[45] Bristol-Myers Co., 85 F.C.T.688 (1975).

[46] Block Drug Co., 90 F.T.C. 893 (1977).

[47] Id. Thompson, dissenting at 902.

[48] Sears, Roebuck, supra note 24.

[49] Id. at 491.

Consider also the case involving Listerine.[50] As noted earlier, in this case the company claimed that the product would prevent colds or lessen their severity. Consumers probably would have been willing to pay some increment more for Listerine if the claims had been true. Certainly, anyone who has suffered the common cold is likely to be willing to pay at least some amount of money to ameliorate or prevent the cold. There was also survey evidence indicating that many consumers thought fighting colds was an extremely important characteristic of a mouthwash. Further, it was difficult for the consumer to evaluate the accuracy of these false claims because most colds are self-limiting and improve without medication.[51] Again, it is difficult to see how an injury test would have significantly complicated this litigation.

Of course, a consumer injury test would eliminate certain cases that should not be brought. It would not, however, substantially complicate those cases when the Commission clearly should act. In cases where it is unclear whether the Commission should act, it is entirely appropriate, in my judgment, to consider external evidence rather than relying on introspection.

Some critics of the standard I recommend have argued that it is insufficiently broad to encompass certain perceived harms. It is argued that the damage caused by a deceptive representation is not confined to the specifically targeted consumer audience. These critics point out that deceptive statements serve to injure competitors and to undermine the credibility of all statements in the market.

All successful advertising, however, injures some competitors. Advertising leads consumers to purchase the advertised product, to the detriment of competitors who produce other brands. A definition of deceptive advertising should include only ads that wrongly divert trade. In a market economy, consumers should decide whether the diversion is right or wrong in the absence of deception. Accordingly, the standard for wrongful diversion should be consumer injury. In other words, the injury to competitors that is relevant for public policy is injury from losing consumers who are injured by another firm's deception.

As an agency, our primary focus always should be on injury to competition and consumers, not injury to specific competitors. The Commission has an important role in protecting consumers from deceptive acts and practices because they generally have no other practical recourse against the resulting injury. Businesses, on the other hand, have other workable remedies to protect them from such harms.[52] Moreover, competitors generally have every incentive to provide consumers with information indicating that their product is better, if such is the case. When there is no likelihood of consumer injury in the process, disputes among competitors are best resolved by the market, not the Commission.

Furthermore, the standard I recommend contains language permitting the Commission to prosecute material representations the advertiser knew or should have known would be misleading. Under this provision the Commission would not be required to show the likelihood of consumer injury. It is intended, in part, to provide strong protection for the credibility of truthful advertising by permitting the Commission to ensure that advertising claims are made with due care.

The injury requirement is proper for other cases. Realizing that the Commission has only limited enforcement resources to devote to policing the marketplace, the superficial appeal of these criticisms of the standard I recommend evaporates. It is true that, to some extent, the dissemination of any claim that is misleading to the ordinary consumer makes all claims—including true ones—less credible. Because, however, this is a harmful characteristic of all misleading representations, it makes sense to devote our scarce enforcement resources to pursuing claims that additionally result in direct consumer injury.

Finally, the types of misleading statements that fail to meet the consumer injury test are not likely to affect the credibility of truthful claims. Many of the claims that would fail the injury test would consist of subjective claims, obviously exaggerated statements, and correctly stated opinions. Generally, these types of claims inherently are incapable of providing the ordinary consumer with misleading information[53] and thus can have no ill effect on the credibility of truthful information. Those types of claims that are in fact misleading and fail the injury test are likely to involve products that are low in price, are frequently purchased, and are easy to evaluate. The marketplace itself is likely to be more effective than the Commission in eliminating such misleading claims.[54]

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[50] Warner-Lambert Co., 86 F.T.C. 1398 (1975), aff'd as modified, 562 F. 2d 749 (D.C. Cir. 1977), cert. denied, 435 U.S. 950 (1978).

[51] See id. at 1462.

[52] For example, §43(a) of the Lanham Trademark Act, 15 U.S.C. 1125(a), enables a competitor to obtain injunctive relief and money damages when rivals falsely advertise their own products to the detriment of the competitor.

[53] See supra, discussion at pages 14–15.

In summary, the statutory definition of deception I recommend would provide more and better consumer protection without a significant increase in the evidentiary burden. By using extreme examples to discourage the enactment of new standards, critics really are suggesting that evidence should not be essential before the Commission acts in cases when it is not clear there has been any wrong to correct. In the strong cases, the standard I recommend would place no significant evidentiary obstacle in the path of effective and efficient law enforcement. But in the marginal case, the Commission would be required to meet evidence against its case with evidence that is even stronger. This, I think, makes eminent good sense.

MATERIAL REPRESENTATIONS THE ADVERTISER KNEW OR SHOULD HAVE KNOWN WERE MISLEADING

Under the standard for deception that I recommend an advertisement could also be found to violate Section 5 if the advertiser knew or should have known that consumers would be misled regarding any material representation—that is, one relevant to the ad's selling purpose. Thus, showing of a likelihood of consumer injury would not be necessary

Prosecution of deceptive practices under the "knew or should have known" standard is sound public policy. It can be presumed that advertising generally benefits consumers, as substantial empirical evidence demonstrates.[55] However, no such presumption exists for advertising that the company knew or should have known was misleading. Because the presumption of benefit disappears in this situation, in such cases the Commission should not be required to show the likelihood of consumer injury.

This provision of the definition I recommend could be used to protect consumers, even if they were not acting reasonably in the circumstances. A major reason for including this second part of the standard is to protect vulnerable groups or consumers who are a minority of the audience. To be candid, I believe that most cases involving vulnerable groups could be pursued under the reasonableness-plus-injury provision just discussed. In some instances, however, the knew or should have known standard will permit prosecution of meritorious cases that could not easily be brought under the reasonableness-plus-injury provision, either because of the difficulty of proving that the interpretation was reasonable or that the representation was likely to lead to consumer injury.

For example, children may be exposed to advertising intended for adults. While a certain advertising message would not be deceptive to reasonable adults, it could mislead children, who are a minority of the audience. Although I would not propose that we protect children by making all advertising understandable to four year olds, in some cases it may be necessary to protect children, or other vulnerable groups, from the consequences of a message that is intended for a larger audience. Thus, where the reasonableness-plus-injury test is inadequate, this provision would allow the Commission to challenge ads that would injure the vulnerable minority.

Under the "knew or should have known" provision, the Commission would not have to show that the advertiser had actual notice that the practice was misleading, or that the advertiser intended the consequences of the particular communication. Rather, it would be sufficient to show that the advertiser should have realized the risk that those consequences might follow.[56]

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[54] See supra, discussion at pages 35–36.

[55] See, e.g., Benham, "The Effects of Advertising on the Price of Eyeglasses," 15 *J. L. Econ.*, 337 (1972); Cady, Restricted Advertising and Competition: The Case of Retail Drugs, Washington: American Enterprise Institute, 1976; Steiner, "Does Advertising Lower Consumer Prices?" 37 J. Marketing, Oct. 1973, at 19, Reprinted by American Enterprise Institute, Jan. 1976.

[56] The Commission has developed experience with this standard over the years. See ITT Continental Baking Co., 83 F.T.C. 865, 868 (1973), aff'd and modified, 532 F.2d 207, (2d Cir. 1976). Some Commission decisions have applied it in assessing the liability of advertising agencies for false ads. The Commission finds liability by examining objective factors relating to the ad agency's degree of participation in the campaign. Quinton Co., 69 F.T.C. 526, 559, modified 70 F.T.C. 45 (1966), aff'd sub nom. *Doherty, Clifford, Steers, & Shenfield,* v. *FTC,* 392 F.2d 921, 928 (6th Cir. 1968). Carter Products, Inc., 60 F.T.C. 782 (1962), modified 323 F.2d 523, 534 (5th Cir. 1963).

Moreover, all of the cases in the defects program except one have pled in the complaints that the manufacturer knew or should have known that the product was likely to experience a particular problem. An investigation considers the information about the problem that was available to the company at the time. Chrysler Corp., 96 F.T.C. 134 (1980; consent order; rust); Chrysler Corp., C–3084 (Feb. 17, 1982; oil filters), American Honda Motor Corp., C–3082, (Jan. 22, 1982), Volkswagen of America Inc., C–3090 (May 24, 1982). No cases in the defects program have been fully litigated to date.

Generally, the "knew or should have known" provision would not impose a greater evidentiary burden than already exists. It is not a criminal standard. It is much more akin to negligence; indeed, "should have known" is the classic tort phrase for negligence.

The Commission's ability to pursue deception cases under the "knew or should have known" provision would provide it with an alternative approach to enforcement, to ensure more efficient and effective consumer protection. The "knew or should have known" provision would allow the Commission to challenge an ad or practice directed to a larger audience that misleads certain members within the larger audience concerning a relevant selling point. The standard is needed in these cases, because when the Commission acts against claims that are deceptive to a small minority, it inevitably restricts truthful and useful information to the majority. The presumption in favor of not tampering with the market process by which useful information is provided to consumers, however, is not justified when it can be demonstrated that the advertiser knew or should have known that consumers would be misled regarding a material representation.

CONCLUDING REMARKS

I realize, of course, that some may agree with the analysis just described but conclude that the most appropriate initiative is for the Commission to adopt the recommended standard as a formal guideline or protocol. In other words, is a statutory standard really necessary?

I believe that a statutory definition of deception is indeed necessary to implement this proposal effectively. A statute, unlike an internal guideline, provides assurance of long-term consistency. The Commission has implemented internal guidelines, policy planning protocols, and other decision-making processes in the past. But too often the Commission has observed these policy standards only in the breach, and in far too many instances uncertainty over the Commission's policy results.

More importantly, I believe that Congress, not a commission of unelected officials, is the proper body to determine the appropriate legal standards. Clear language incorporated into the Federal Trade Commission Act will be a statement of the agency's mission. It will tell the Commission what the American people want it to do, and equally important, clear language will tell us what the American people do not want us to do. A statutory definition will promote accountability to the public. Without specific language, there is little or no accountability because the Commissioners decide for themselves how they want to use their broad discretion. And when the composition of the Commission changes, so too do the standards.

Moreover, a statutory definition will facilitate judicial review. Courts routinely defer to the decisions of the Commission regarding deception. This is one reason why "the Commission has managed to prevail in the appellate courts in the overwhelming majority of its [deception] decisions that have been appealed."[57] A statutory definition will provide guidance to the courts by spelling out the standards upon which their review should be based.

Any change or any legislation, or course, can itself increase uncertainty. This potential for uncertainty is not now nor has it ever been a reason to avoid justified change, especially in an area when the results under the present statute have themselves caused uncertainty.

Some argue that courts will interpret a statutory amendment as requiring deviation even from the reasonable results found in prior cases. This fear is groundless. A statutory amendment would not in any way mean that years of reasonable decisions benefitting consumers would be lost or ignored. Although there is a general presumption of change when a statute is amended,[58] amending acts "do not change existing law further than is expressly declared or necessarily implied."[59] There is no basis in either law or common sense for the suggestion that an amendment to a statute calls for results opposite from those decided under the unamended version. Of course, there will be some cases that will lose their persuasive value as precedent under the new standard, but in my judgment those are the cases in which consumers were injured rather than protected, and the Commission's resources were squandered.

In short, the propsed standard will greatly alleviate, if not eliminate, the many problems arising under the current statute with its lack of explicit standards. The absence of a clear definition of deception has resulted in cases that are often cited to illustrate the Commission's inappropriate use of its discretion. Even more importantly, the proposed standard will correct the inadequacy of the present statute under which consumers and businesses have been injured, rather than protected.

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[57] Pitofsky, supra note 7, at 677-78. See also Rosden, supra note 1.

[58] 1A Sutherland, Statutes and Statutory Construction, § 22.30 (Sands ed. 1973).

[59] Id.

Mr. Chairman and Members of the Subcommittee: that completes my prepared statement. I shall be pleased to address any questions you might have.

[The following information was subsequently received for the record:]

QUESTIONS OF THE COMMITTEE AND THE ANSWERS THERETO

Question 1. Consumers Union has criticized your discussion of the cases you relied on in your earlier testimony before this Committee. Please provide your comments on these criticisms.

Answer. Consumers Union has criticized my discussion of past Commission cases by making a number of widely varying arguments. These arguments are often case specific, and therefore, rather than provide a generalized answer, I have prepared separate comments on CU's criticisms for each case. These specific comments are attached as Appendix A.

It is noteworthy that CU concedes that many of the cases I have discussed do not represent the best allocation of Commission resources. In other cases, CU argues that while the Commission may have brought certain unreasonable charges, they were at least joined in the complaint with charges that properly should have been brought. The fact that the current statute permits the misuse of scarce Commission resources on strained or unreasonable interpretations of claims or cases where injury is unlikely is reason for change. Even where the cases discussed are justified on the basis of other claims or circumstances, the Commission's unreasonable pursuit of harmless claims wastes resources. It can also set bad precedent, thereby discouraging claims that are useful to consumers. Consequently, the proposed statutory change is desirable to avoid wasting resources and to avoid setting undesirable precedents.

Question 2. What effect would your proposed definition have on state enforcement under so-called "little FTC acts?"

Answer. While I would commend to the states the virtues of statutorily defining the term "deceptive acts or practices," I recognize that some may disagree with my proposal as a prescription for state regulation. The beauty of our federal system is that it allows room for experimentation and variety, to suit the viewpoints of different groups. In this regard, I am convinced that the statutory definition of deception would have no significant impact upon those states that wish to adhere to prior constructions.

A review of the relevant statutes reveals that all 50 states, the District of Columbia, Guam, Puerto Rico, and the Virgin Islands—54 jurisdictions in all—prohibit deceptive, false, misleading or fraudulent trade practices. In seven of those jurisdictions, however, this term is expressly limited to an itemized list of practices,[1] and so the term "deceptive" is already defined in these states and could not even arguably be affected by changes at the federal level.

Of the 47 jurisdictions that have "catch-all," or omnibus, prohibitions against deceptive practices, in 27 of them the law specifically provides that state courts shall look to "interpretations" of the Federal statute in construing state law. Twelve jurisdictions provide for a specific exemption from the statute, or a defense, for acts or practices permitted by or in compliance with the rules or regulations of, or statutes administered by the FTC.[2] The statutes in the other eight jurisdictions make no reference to Federal law.[3]

In none of the jurisdictions, however, where the statute expresses the legislative intent that the courts look to interpretations of the Federal statute for guidance, will the administering official or the courts be bound to follow interpretations of an amended section 5. First, an Attorney General seeking to enforce the law would find substantial support for arguing that where the legislature has passed one statute which makes a cross-reference to a second statute, it refers only to the language of that second statute as it existed at the time the first statute was passed.[4] Moreover, while interpretations of Federal law may be consulted for guidance and may be persuasive where the state law prohibits deceptive practices without defining those practices, the administering officials or courts are not bound to follow even those interpretations that existed at the time the state law was enacted.[5]

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[1] Colorado, District of Columbia, Indiana, Mississippi, Nevada, Oklahoma, Wyoming.

[2] Arizona, Arkansas, Delaware, Idaho, Iowa, Louisiana, Missouri, New Jersey, New York, Ohio, South Carolina, and Texas.

[3] California, Michigan, Nebraska, North Carolina, Oregon, Pennsylvania, Puerto Rico, and Wisconsin.

In those jurisdictions where the law provides for an exemption or defense for acts or practices permitted by or in compliance with the rules or regulations of, or the statutes administered by, the FTC, it is those rules or regulations and statutes that existed at the time of enactment of the state law that would be relevant. A statutory exemption which swept in future federal rules or regulations or statutes would conflict with provisions in state constitutions. Such open-ended exemption have been deemed to be an impermissible delegation of the state legislative authority to a body outside the state.[6]

In short, my proposed definition of "deceptive acts or practices," need not in any way alter the construction of those terms at the state level, absent a conscious and voluntary election to effect such a change. I have attached a memorandum prepared by the Commission's General Counsel's Office that analyzes in detail the relationship between the Federal Trade Commission Act and the "little FTC Acts" and the impact of the proposed amendments to section 5 on state enforcement. (Appendix B).

Question 3. How would your proposal alter the law of deception by omission? Would it be possible for the Commission to proceed against land sales when the seller fails to disclose that the land is under water under your definition? Would it be possible to require health warnings in cigarette advertising?

Answer. The statutory proposal defining deception would permit the Commission to require affirmative disclosures when necessary to prevent a material representation from misleading consumers. The proposed reasonable interpretation standard is concerned with the effect of an advertising claim on the beliefs of consumers, acting reasonably in the circumstances. An advertisement may be literally true but still lead many consumers to draw false inferences about a product; this has the same effect as if the false inferences had been stated explicitly. In such a case, deception may occur through the advertiser's failure to disclose the information necessary to prevent consumers from forming the false beliefs.

For example, a seller may claim that a product "kills bacteria that cause baldness." This statement may be literally true, but deceptive to the vast majority of men whose baldness is due to hereditary factors. A strictly literal reading of this claim would not lead the consumer to jump to the inference that the product will be effective in curing his baldness. Whether an advertisement misleads consumers to their detriment, however, depends not on the formal rules of semantics and logic but on what message the advertisement conveys to the typical member of the target audience. Because the reasonable consumer is likely to respond to the "kills bacteria that cause blindness" claims by forming the natural but inaccurate belief that the baldness cure will be effective treatment for his baldness, it would be deceptive for the advertiser to fail to disclose that most baldness is due to hereditary factors. See Ward Lab., Inc. 55 F.T.C. 1337 (1959), 276 F.2d 952 (2d Cir), cert. denied, 364 U.S. 827 (1960). Thus, whether the statutory proposal would permit the Commission to proceed on deception grounds against sellers of land, cigarettes, or any other product for failing to disclose certain information depends on whether affirmative disclosure is necessary to correct any false belief otherwise formed or reinforced in reasonable consumers by the advertisements under consideration.

Even when deception is not available to require an affirmative disclosure, under my proposals the Commission could still seek disclosure under an unfairness theory. Disclosure would be appropriate if the benefit/cost criteria outlined in the Commission's March 5, 1982 letter to Senators Packwood and Kasten were met.

Question 4. Has your proposal changed significantly since you first raised it? Have you dropped the blanket exemption you originally proposed for correctly stated expert opinions?

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[4] *Department of Legal Affairs* v. *Lee Roger d/b/a American Holiday Assoc.*, 329 So. 2d 257, 267 (Fla. 1976); *see generally*, 2A Sutherland, Statutes and Statutory Construction, § 5107 (Sands ed. 1973) and *Hassett* v. *Welch*, 303 U.S. 303 (1938).

[5] See, e.g., *North Carolina ex rel. Rufus L. Edmisten, Attorney General* v. *J. C. Penney Co.*, 292 N.C. 311, 233 S.E. 2d 895 (1977); *Wisconsin* v. *Amoco Oil Co.*, 97 Wis. 2d 226, 293 N.W. 2d 487, 493 (1980); *Island Tobacco Co.* v. *R. J. Reynolds Tobacco Co.*, 627 P. 2d 260, 269 (Haw. 1981); *Washington* v. *Ralph Williams NorthWest Chrysler Plymouth, Inc.*, 82 Wash. 2d 265, 510 P. 2d 233, 238 (1976); *Gour* v. *Daray Motor Co., & General Motors, Inc.*, 373 So. 2d 571 (La. App. 1979).

[6] See, e.g., *Department of Legal Affairs* v. *Lee Roger d/b/a American Holiday Assoc.*, supra, and *Johnson* v. *State*, 227 Ga. 181, 387, 181 S.E. 2d 42 (1971).

Answer. Although I have explained my reasons for supporting a statutory definition of deception on many occasions and have appreciated those opportunities, my position concerning proper public policy in this important area of consumer protection has not changed. In February, 1982, I proposed in writing to my fellow Commissioners that a deceptive act or practice should be defined as "One that is a statement or representation of fact: (a) that its perpetrator knew or should have known was false or misleading; or (b) by which a consumer, acting reasonably in the circumstances, is likely to be misled to his detriment." This language is virtually identical to that proposed in my July testimony.

The common law distinction between fact and opinion arose because reasonable consumers do not rely on clearly identified opinions as fact. As the courts have recognized, the issue is not simply resolved by the form of the statement; rather, it is a question of reasonable interpretations of the statement. Thus, because reasonable consumers interpret claims about opinions and facts differently, the resasonableness standard I propose incorporates the essence of the common law distinction. A separate exemption for opinion claims is therefore unnecessary.

Nonetheless, the standard I propose protects correctly stated expert opinions, as I believe it should. Correctly stated and accurately understood expert opinions give consumers access to valuable information about the conclusions of those more knowledgeable at low cost. Consumers are not deceived by these types of statements, because they contain all the information necessary for consumers to make their own evaluation of the significance of the opinion. Conversely, misrepresentations of opinion can injure consumers and would be subject to challenge under the proposed statutory definition of deception. Express or implied misrepresentations that a person holds an opinion when in fact he or she does not, that the opinion is held more extensively than in fact is the case, or that the opinion holder possesses expertise when he or she does not, all may mislead reasonable consumers to their detriment.

Question 5. What would be the impact of your proposal on the Commission's advertising substantiation program? Suppose an advertiser made an unsubstantiated, but scientifically testable claim that a new drug "cured 80 percent of all cancer"; how would your proposed requirements for reasonable reliance and consumer injury apply to this lack of prior substantiation?

Answer. A carefully applied substantiation requirement is fully consistent with the proposed statutory definition of deception. As former Chairman Collier testified before this committee, it is reasonable to interpret most factual advertisements as containing an express or implied claim that support exists for the advertised product characteristic. Reasonable consumers are likely to rely on claims they recognize as groundless. Because the advertiser's purpose is to persuade consumers to purchase its product in reliance on its specific claims about the product's attributes, the advertiser plainly desires to convey the message that support exists for those claimed attributes. Therefore, I agree in principle with the Commission's statement in National Commission on Egg Nutrition:

> Many consumers are likely to assume that when a product claim is advanced which is in theory subject to objective verification, the party making it possesses a reasonable basis for so doing, and that the assertion does not constitute mere surmise or wishful thinking on the advertiser's part. 88 F.T.C. 89, 191 (1976), modified, 570 F.2d 157 (7th Cir. 1977), cert. denied, 439 U.S. 821 (1978).

In the hypothetical example presented, the specificity and nature of the claim that a new drug "cured 80 percent of all cancer" clearly implies that the claim is supported by a reasonable basis. It seems reasonable for consumers to infer that ads stating figures suggesting test results in fact are supported by tests. It is surely not reasonable to expect consumers to infer that such a specific claim was picked out of thin air.

Again, as former Chairman Collier testified, express or implied support claims can be material to consumer purchasing decisions. Support claims that are truthful and accurately understood provide consumers with extremely valuable information concerning the likelihood the product will in fact have the advertised characteristics or benefits desired by the purchaser.

Question 6. You would apparently still permit the FTC, in appropriate cases, to determine the reasonableness of ad claims and the likelihood of consumer injury from the ad itself, without extrinsic evidence. How would the FTC and the courts decide which cases would require extrinsic evidence?

Answer. I believe that extrinsic evidence will be required only in close cases. Specifically, extrinsic evidence would be required in cases where the meaning of an ad to a typical consumer is unpredictable or where the likelihood of injury is difficult to determine. In many instances, the meaning of a representation to the typical consumer is likely to be apparent on the ad's face and the representation itself may be the only evidence necessary. Where an ad is capable of multiple, plausible interpretations, not all of which may be deceptive, extrinsic evidence would be necessary in order for the Commission to find how the ordinary consumer would interpret the challenged representation. For instance, in Kroger, without any evidence about the ad's meaning, the Commission held that the ads implicitly represented that the advertised comparative food price surveys were "methodologically sound" and "statistically projectable." Kroger Co., D. 9102 (Sept. 25, 1981), appealed docketed, No. 81-7937 (11th Cir. Nov. 23, 1981). Commissioner Bailey dissented and wrote she believed these findings were an artificial construct imposed by the majority. (Id., Bailey, dissenting at 3). In this case, under the proposed standard, extrinsic evidence about the ad's meaning would have been required. Although obtaining extrinsic evidence necessarily involves some costs, those costs are far less than the costs to taxpayers, advertisers, and consumers of pursuing strained or unreasonable interpretations of ads.

Similarly, the requirement that the Commission find that the challenged practice is likely to result in consumer injury is beneficial and workable. As with the reasonableness requirement, inferences about the likelihood of injury frequently will be the only evidence necessary, because the key question is whether consumers have given up something of value by their reliance on the misleading claim. For instance, when an advertiser claims that a product has a certain feature that consumers would like, we can normally assume that the product is worth more to consumers if the claim is true. Even when the price of the product with the deceptively advertised feature is the same as those products without the feature, injury can be inferred. In some cases, consumers give up the opportunity to purchase another brand that actually provides the advertised feature. In other instances, consumers may have preferred to spend their money on some other product if they knew that the advertised feature was not actually available. There is injury in such cases because consumers give up a valuable alternative by purchasing the deceptively advertised product.

Consequently, requiring that the likelihood of injury be shown frequently can be accomplished through inferences that will not substantially complicate those cases when the Commission clearly should act. But, where it is unclear whether consumers have given up something of value in reliance on a misleading claim, extrinsic evidence of consumer injury should be necessary. Thus, for example, I believe the standard would require extrinsic evidence of the likelihood of injury in cases where the representation concerns a product that is inexpensive, frequently purchased and easy for consumers to evaluate.

Question 7. Is there a difference between "unfair" and "deceptive" advertising? Are these separable legal concepts?

Answer. Under current law, there is little, if any, difference between unfairness and deception. Virtually any action the Commission has taken under its unfairness authority also could be taken under current theories of deception. It is for this reason that I have proposed a statutory definition of deception, to complement the definition of unfairness recommended by the Commission and the Senate Commerce Committee. Without such action, Congress may well find that its unfairness definition has no effect, because the Commission can bring the same cases and rulemaking proposals under a deception theory.

Unfairness and deception, however, should be separate and distinct legal concepts. Deception should address practices that involve a representation that misleads reasonable consumers to their detriment, whether that representation is express or implied, or representations that the advertiser knew or should have known would be misleading. Unfairness is a broader concept, that should be used to reach acts or practices that do not involve misleading representations, but nevertheless injure consumers. For example, the market may fail to provide information that would enable consumers to avoid some injury. When the benefits of providing such information exceed the costs, the Commission should be empowered to act to assure its availability.

QUESTIONS OF THE MINORITY AND THE ANSWERS THERETO

Question 1. In the area of deceptive acts or practices, since you have been on the Commission, has any proposed complaint come before the Commission or been issued by the Commission which you feel does not meet the criteria you set out in your testimony?

Answer. Since I have been Chairman, I have been convinced that all the proposed or issued complaints before the Commission regarding deceptive acts or practices have provided some reason to believe that the standards described in my testimony have been met. I believe this is due, in large part, to internal guidelines and to the efforts of the Commission's current Bureau Director and staff. It would be inappropriate to discuss those matters further since they are in litigation.

Despite the recent success of the internal review process, I firmly believe a statutory definition is necessary. A statute, unlike an internal guideline, provides assurance of long-term consistency. The Commission has had internal guidelines, policy planning protocols, and other decision-making processes, but these do not eliminate costly uncertainty. Furthermore, Congress is the proper body to determine the appropriate legal standards, not an agency of unelected officials. A statutory definition will promote accountability to the public. Without specific language, there is little or no accountability because the Commissioners decide for themselves how they want to use their broad discretion. And when the Commissioners change, so too do the standards. Lastly, a statutory definition has the benefit of facilitating judicial review. By providing the standards upon which they can base their review, a statutory definition will assist the courts in determining the propriety of Commission decision-making.

Question 2. Should advertising that will mislead a small minority of consumers to their great detriment be policed?

Answer. The proposed statutory deception standard has been devised carefully to ensure that all of the many diverse groups of consumers in our society are fully protected from injury. Because the reasonable interpretation standard focuses on the perceptions of the target audience, an advertisement that is relevant to a particular group is evaluated against the circumstances—no matter how unusual or special—of that group, including age, sophistication and special vulnerabilities. Thus, for example, a product that claims to be a miracle cure for terminal cancer victims is not likely to have substantial appeal to other groups and should be judged against the standards of reasonable interpretation given that the audience is terminally ill. Although the ordinary person without health problems might be likely to reject miracle cure claims as unbelievable, the reasonable interpretation standard would require the Commission to consider the desperate condition of the target audience in interpreting the message the ad conveyed.

In some cases, however, it may be necessary to protect children, or other vulnerable groups, from the consequences of a message that is intended for a larger audience. The alternative "knew or should have known" standard in the proposed deception definition provides this protection. For example, children may be exposed to advertising intended for adults. Although a certain advertising message would not be deceptive to reasonable adults, it could mislead children, who are a minority of the audience. In that case, if the advertiser knew or should have known that children would be mislead, the claim could be actionable. Thus, when the reasonableness-plus-injury test is inadequate, the knew or should have known standard would allow the Commission to challenge ads that are not determental to the majority, but greatly injure the minority.

(APPENDIX A)

Responses to C.U.'s Criticisms of Cases Relied On By Chairman Miller in his testimony before the Senate Committee on Commerce, Science, and Transportation. March 18. 1982.

Kroger Co., D. 9102 (Sept. 25, 1981), appeal docketed, No. 81-7937 (11th Cir. Nov. 23, 1981) (food price survey).

C.U.'s Criticism: (1) Chairman Miller's reference to commissioner Bailey's dissent in the case only shows that reasonable commissioners can differ and not that the Commission should not be permitted to rely on its experience or expertise in determining the deceptive capacity of an ad.

Response: (1) Commissioner Bailey's dissent on the meaning of the ads merely illustrates the Commission's reliance on its presumed expertise where the meaning of a representation to the typical consumer is not apparent on the ad's face. Under such a circumstance, the interpretation of ads should not be left to the subjective judgments of the Commissioners, who almost always have no special background in advertising or communication. With a reasonableness standard as part of the statute, the Commission would be asked to base its interpretations on facts.

C.U.'s Criticism: (2) According to the testimony of three experts, there was a potential for bias in the survey because the Kroger official who composed the Price Patrol marketbasket sample also handled discounts from the firm's suppliers and selected price leader items for Kroger's advertising.

Response: (2) Kroger had good reasons for conducting the survey as it did. Judgment samples were essential, because not all stores carry all items. Samples must be selected by someone with enough knowledge of the business to insure that most of them are available at most stores. The only Kroger employees with such knowledge were the merchandisers, who also set the prices. Any other alternative would be quite costly. Moreover, Kroger acted to minimize the potential problems. The grocery merchandiser selected 600 items, which were divided into four lists for weekly use by the price patrollers. The merchandiser did not know when any given item would appear in the survey. The insignificance of any actual bias is indicated by the Commission finding that Kroger's prices were frequently below or equal to its competitors.

C.U.'s Criticism: (3) Kroger possessed two private surveys more scientifically composed and with larger samples than the Price Patrol surveys. Since Kroger lost to the competition more often in these than in the informal surveys, the information Kroger advertised could have misled the public.

Response: (3) These surveys support Kroger's claim that its prices were generally lower. In one survey, the total dollar cost of shopping at Kroger was lower than the competitor in 92 percent of the individual comparisons. In the other, Kroger had more items with lower prices than the competitor in 93 percent of the comparisons.

Block Drug Co., 90 F.T.C. 893 (1977) (misleading dental adhesive performance claims).

C.U.'s Criticism: Consumers Union argues that the consumers were injured by the Poli-Grip claim by having to make the initial purchase in order to discover the deception.

Response: In order to make this decision binding on its competitors, Block agreed to try the case on stipulated facts. Thus, whether the ALJ or the Commission would have found the ads deceptive is uncertain. In cases where the product is low priced, frequently purchased and easy to evaluate it is extremely unlikely there will be any deception, because there is no incentive to mislead. Although consumers may purchase the product once, they will not do so again. Thus, the returns from a single purchase are unlikely to cover the costs of disseminating the false advertising. In short, the market works—deception is not a viable business strategy.

As to consumer injury, this is measured by the value of what consumers give up by relying on the misleading claim. In the Poli-Grip case, most denture wearers use denture adhesive anyway. Thus, at worst, any injury is the difference in price between Poli-Grip and other denture adhesives on a one-time purchase basis. Indeed, Consumers Union contends that competitors commonly were making the same type of performance claims as those made by Poli-Grip. If this is the case, it was impossible for Block Drug to demand a premium for Poli-Grip based on the misleading performance claims. Thus, there was no consumer injury. Consumers Union understates the case in conceding that the Commission might have found better uses for its enforcement resources than pursuing the Poli-Grip claim.

Ford Motor Co., 87 F.T.C. 756 (1976) (performance claim concerning automobile gas mileage).

C.U.'s Criticism: Consumers Union argues that our reading of this case is incorrect. It contends that the administrative law judge considered the Ford survey and that the issue of the survey's weight as evidence was not before the Commission on appeal.

Response: Consumer Union's reconstruction of this case is plainly wrong. It is true that the Administrative Law Judge spent a brief two paragraphs opining that some individual interviewee responses in the Ford survey were consistent with the "average driver" meaning attributed in the complaint to the advertisement. The administratrative law judge, however, entered a summary decision against Ford, without considering the testimony of Ford's experts interpreting the survey results. On appeal, Ford specifically argued that the Administrative Law Judge erred in refusing to consider Ford's experts' testimony before entering a decision. The Commission rejected Ford's argument, and stated:

"The Commission is not required to survey public opinion to determine what the Ford ads represent to the public; nor is it bound to review respondents experts' testimony based on consumer survey data, which constitutes a surrogate form of direct consumer testimony." 87 F.T.C. at 756.

Levitz Furniture Corp., 88 F.T.C. 263 (1976) (deceptive pricing).

C.U.'s Criticism: (1) Consumers Union concedes that "[t]hese kinds of cases may not be the best allocation of the FTC's resources." It argues, however, that these practices should be considered deceptive because they may often lead to bait and switch sale situations involving additional oral representations at the point of sale.

Response: (1) It is difficult to see how the practices in this case have anything to do with "bait and switch" practices. It is one thing to misrepresent the sale "savings" on an item and quite another to misrepresent the actual selling price or to misrepresent that an item is in stock. In the latter two cses, but not the former, consumers suffer actual injury. They suffer the costs involved in traveling to the advertiser's business in reliance on a misleading claim that they can purchase a product at a specific price when, in fact, they can not. Moreover, "bait and switching" would be actionable in all cases where additional point of sale representations were made that would mislead reasonable consumers to their detriment.

C.U.'s Criticism: (2) CU further contends that consumers may be less interested in the actual selling price information contained in an advertisement than in determining which advertisers have comparatively low prices.

Response: (2) Fictitious price claims that exaggerate the price against which the discount is compared, do not injure consumers as long as they are accurately informed of the selling price. Indeed, often times, exaggerated discount or sales claims provide consumers with a signal that the advertiser emphasizes price rather than service or reliability. Thus, contrary to the CU criticism, such claims can provide useful comparative pricing information, broaden consumer choice and stimulate competition. As former Commissioner Pitofsky has stated:

> [M]uch fictitious pricing enforcement entails considerable social and economic costs. A natural target for such enforcement has been discount houses, and the usual complainants have been nondiscounters who emphasize service and reliability rather than price. Aggressive enforcement against discounters that forces them to hew close to the line of accurate information may tend to dampen competitive activity. Often, "cents-off," free goods, couponing and other discount promotions are devices that assist new entrants in penetrating concentrated markets and that tend to unsettle stable and rigid pricing patterns. Couponing and free goods may be the only legal way that a seller can effectuate a price cut to consumers when intermediate distributors refuse to pass along a list price reduction. While the same pro-competitive effects can be achieved by accurate price claims in connection with these promotions, the cost to sellers of ascertaining whether particular discount claims are accurate may deter them from making such claims at all.

Beyond Nader: Consumer Protection and the Regulation of Advertising, 90 Harv. L. Rev. 661, 688 (1977) (note omitted.)

Nagle, Spillman & Bergman, Inc., 88 F.T.C. 244 (1976), and Morton-Norwich Products, Inc., 86 F.T.C. 299 (1975) (failure to disclose salt substitute's contraindicated usages).

C.U.'s Criticism: In these cases, Chairman Miller criticized the Commission for requiring a disclosure that potassium chloride products sold as salt substitutes should not be used by those on postassium restricted diets. C.U. objects that Chairman Miller has taken the Commission charges out of context and that he fails to state objectively why a failure to disclose requirement is inappropriate in these cases. C.U. responds to Chairman Miller's objection to the Commission's challenge of the tastes like salt claim by stating that the Commission probably would not have challenged the taste claim alone.

Response: There is no implication from these ads that using the salt substitute would be advisable for everyone under all circumstnces, including people who must restrict their potassium intake. If the Commission can require disclosure based upon deception when there have been no false implications to deceive consumers, then what could the Commission not do under its deception power? Even if such implications could be found, it is likely that people on potassium restricted diets have talked to their physicians, and would not rely on those claims. (That is not to say, however, that disclosure should not be required under unfairness theory, which requires a careful balancing of the benefits and costs of the additional information or that warnings should not be required on the labels.) In addition, it is important that the Commission not discourage advertisers from informing consumers about emerging scientific evidence on the health problems connected with the excess consumption of salt. As for the tastes like salt claim, the Commission's challenge is illustrative of the potential for other needless challenges in the future.

General Motors Corp., 85 F.T.C. 27 (1975) (Road & Track's opinion about Vegas was inadequate substantiation) (consent order).

C.U.'s Criticism: (1) In this case, General Motors advertised that Road and Track magazine found the Vega to be the best handling car ever built in the U.S. The Commission interpreted GM's claim to mean Vega really is the best handling car found that Road and Track magazine was not adequate substantiation for that claim. Consumers Union takes issue with the judgment that the Commission interpretation of this advertisement probably was unreasonable.

Response: (1) Even if reasonable consumers did interpret the ad as a claim that Vega really is the best handling car, Road and Track should have been adequate substantiation for the claim, because the substantiation was disclosed in the ad. The result of the order in this case was to deprive consumers of valuable opinion information from a reputable publication. The handling performance of automobiles is a subjective quality and is extremely difficult to measure. When a advertiser states an opinion about handling, it is merely inviting consumers who are looking for a car with good handling to test drive the automobile. The typical consumer would interpret such a claim as an invitation to evaluate the product, not as a claim upon which to make an irreversible commitment. In the General Motors ad, in fact, it is expressly stated:

"There's only one way, really to find out what a Chevy Vega is all about, and that's to drive one."

C.U.'s Criticism: (2) Consumers Union generally argues that properly stated opinion information provides a loophole for advertisers to shop around for someone who will state an unsubtantiated performance claim in opinion form.

Response: (2) A reasonableness standard does not permit unscrupulous advertisers to dress up misleading statements in the guise of opinion. A representation of an opinion is a factual claim that the person or institution holds the advertised opinion. Misrepresentations of the opinions of others are clearly subject to challenge. Similarly, it is quite possible to misrepresent the degree of expertise of the source of an opinion. E.g., Leroy Gordon Cooper, 94 F.T.C. 674 (1979) (By endorsing an automotive product, Cooper, an astronaut, represented that he was a trained and knowledgeable expert in automotive engineering). It also should be clear that an advertising claim about the extent of expert opinion is a factual claim. A claim that all experts believe X is actionable if they do not. When a claim uses an expert's opinion in such a way that reasonable consumers would conclude that all experts agree, again there is a misrepresentation of fact that is actionable. This was the situation in the National Commission on Egg Nutrition case, in which the Commission challenged claims that there is "no evidence" linking eggs to heart disease. What is prohibited, however, is misrepresentations about the amount of evidence, not accurate statements of the opinions of various experts.

Spiegel, Inc., 82 F.T.C. 20 (1973), 494 F. 2d 59 (7th Cir. 1974), cert. denied, 419 U.S. 896 (1974) (ads found to falsely imply unconditional offer).

C.U.'s criticism: C.U. has characterized Spiegel as "another false pricing case." C.U. then refers to its criticism of Levitz, contending that the same points would apply to Spiegel.

Response: C.U. is clearly in error in its characterization of this case. In its advertising, Spiegel offered products on a 30 day trial basis or at a percentage off. It is therefore not a false pricing case, but rather one in which the FTC alleged that the ads created the impression that the offer was unconditional, when in fact the consumer had to meet credit qualifications.

Spiegel required consumers to submit credit data with an order, and disclosed that the offer was subject to credit approval. It is difficult to imagine how any reasonable consumer would expect a seller to simply ship goods unconditionally with no assurance of payment in the future.

Brite Mfg., 65 F.T.C. 1067, aff'd, 347 F. 2d 477 (D.C. Cir. 1965) (failure to disclose foreign origin of watch bands prior to sale).

CU's Criticism: (1) Consumers' preference for domestically produced goods was not a "presumption" of the Commission, but a preference which existed for many years among a substantial portion of the public.

Response: (1) This case is cited as an example where the Commission relied on its expertise regarding consumer beliefs to find consumers believed products were of domestic origin, unless otherwise indicated, and that consumers preferred domestic products over foreign ones. It is clear that the respondent would not have been prosecuted for failure to disclose the foreign origin of a part of the product he sold, were it not for these presumptions about consumers' beliefs and preferences.

These cases all have been widely criticized as a misuse of the Commission resources. As Professor Posner has noted, "these cases appear to have nothing to do with supplying information that consumers require in order to make value-maximizing purchases." Regulation of Advertising by the FTC, AEI 1973, at 19.

CU's Criticism: (2) Chairman Miller previously characterized this case and similar cases as ones the Commission should not bring because their purpose was to correct consumers' misimpressions that domestic items are better. Apparently, because it is inconsistent with a belief in consumer sovereignty, he has abandoned that characterization.

Response: (2) Urging that the Commission consider the likelihood of injury rather than just presuming potential injury is fully consistent with consumer sovereignty. Indeed, it assures that the Commission will only act when consumers would consider the result worthwhile.

Dannon Milk Products, Inc., 61 F.T.C. 840 (1962) (food ad found to make factual, not puffing claim).

C.U.'s Criticism: Chairman Miller criticized the Commission for challenging a puffing claim ("Nature's perfect food that science made better") as a factual claim. This characterization takes the case totally out of context, since the respondent also falsely promoted its product as a prevention or cure for various digestive disorders.

Response: The fact that the case was justified on other grounds does not obviate the fact that one of the claims challenged was a puff. This is a classic example of the kind of claim that typical consumers understand is not to be interpreted literally. Dannon could have been brought solely on the basis of the therapeutic claims and the Commission would not have wasted resources needlessly challenging the puffing claim.

Mohawk Refining Corp., 54 F.T.C. 1071 (1958), aff'd, 263 F.2d 818 (3d Cir.), cert. denied, 361 U.S. 814 (1954) (rerefined oil).

C.U.'s Criticism: Chairman Miller's criticism that the virgin and rerefined oil performed equally well is irrelevant since the point of the case was that consumers preferred virgin oil and that if sellers did not disclose that fact to the public they were being allowed to substitute their judgment for that of the buyers.

Response: In this case the Commission excluded evidence regarding the quality of the respondent's motor oil on the basis that it was not material to the issues of the proceeding. This information is, however, material to the issue of whether injury is likely to occur.

Moreover, this case involves omitted information, not any misrepresentation of the properties of the oil. Although the Commission should protect affirmative claims about characteristics that matter to consumers, it should not require disclosure where there is evidence that the difference would not matter to most consumers. To take a different example, although the Commission should challenge false claims that a product is "kosher," it should not require non-kosher products to disclose that fact.

If reasonable consumers were willing to pay more for virgin rather than rerefined oil, knowing that they performed the same, then the principle of consumer sovereignty dictates they should not be denied that choice and the Commission could appropriately take action, under the proposed reasonableness-plus-injury standard.

Liggett & Myers Tobacco Co., 55 F.T.C. 354 (1958) (cigarette ad claimed, inter alia, that it was always milder).

C.U.'s Criticism: Chairman Miller criticizes this case because the consumer is in a position to judge whether the claim of "always milder" is true. Since the claim was perceived by consumers who read the ad to relate to physical irritation rather than taste, it is not solely a subjective judgment. Also, the final order was partially based on expert medical evidence that the claim could not be a substantiated.

Response: Whether "always milder" refers to taste or a physical condition, consumers can judge the truthfulness of the claim themselves. However, my criticism of this claim does not mean that case was a bad one. On the contrary, the Commission properly pursued the ad claim that a study by a medical specialist concluded that "Nose, Throat, and Accessory Organs—Not Adversely Affected by Smoking Chesterfields". Unlike the "always milder" claim, consumers could not judge the truthfulness of the "no adverse effect" claim themselves. The study in question was found to be severely flawed and to have little probative value as a scientific test.

Gelb, 33 F.T.C. 1450 (1941), aff'd as modified, 144 F.2d 58 (2d Cir. 1944) (permanent hair color).

Sebrone Co., 34 F.T.C. 1126 (1942), aff'd, 135 F.2d 676 (7th Cir. 1943) (Deodorant—destroys odors).

C.U.'s Criticism: Both cases are forty years old. Presumably, CU means it is unreasonable to cite them as examples of bad cases that the Commission has brought.

Response: Although these cases are old, they serve to illustrate the wide discretion available to the Commission. Because of the lack of standards and guidelines in the statute, the Commission has continued to bring bad cases, as the more recent examples indicate.

Standard Oil Co. of California, 84 F.T.C. 1401, modified, 577 F.2d 653 (9th Cir. 1978) (claims that a gasoline additive would reduce air pollution).

C.U.'s Criticism: Chairman Miller criticized the Commission for challenging a claim that a motor gasoline additive would cause the disappearance of virtually 100 percent of exhaust emission pollutants and cited the Court of Appeals which reversed this claim. The Chairman's criticism is unfounded because the Court found that the Commission's opinion made a different point (i.e. concern about the ad's implicit statement about the degree of reduction in auto emissions) and upheld the Commission's finding that the 3 ads were misleading.

Response: This claim is cited as a criticism of the Commission's interpretation of the visual demonstration in one of the ads on which the case was predicated. The Court of Appeals did not believe that reasonable consumers observing that demonstration would believe that virtually 100 percent of the pllutants had been eliminated. The Court, however, chose to characterize the Commission's findings as concerning the degree of reduction in auto emission and the effect of that reduction on the pollution problem. As a result, the court held that the 3 ads were misleadfing. Criticism of the Commission's interpretation of the demonstration does not mean that the ads were not misleading in some way or that this was a bad case overall.

Trans World Accounts, Inc., 90 F.T.C. 350 (1977), modified, 94 F.T.C. 141, further modified, 94 F.T.C. 1051, aff'd in part and rev'd and remanded in part, 594 F. 2d 212 (9th Cir. 1979) (debt collection agency's statement that failure to pay prompty may result in imminent commencement of litigation deceptively implies legal action will be taken).

C.U.'s Criticism: Chairman Miller states that the decision was in error and stated the Court of Appeals reversed the FTC's restrictions on the firm's use of the word "may." In fact, the Court upheld the finding of liability and only reversed the order's restrictions on the future use of the world "may."

Response: The statement of this case is consistent with CU's. It indicated that the Court upheld the finding of liability and that the reversal referred to the Commission's restrictions of the use of the word may. The point of this case is that the Commission's interpretation of the word "may" was strained and not one that reasonable consumers are likely to reach. Commissioner Collier's dissent emphasizes the relationship between the order provision and the finding of liability stating:

In deciding for liability, the majority gives "may" a statistical meaning that runs against common usage. Although the majority purports to do this only for the sake of clarifiying the order, it is clear that this statistical conception of "may" is the root of its finding of liability. The work "may" usually conveys uncertainty of a fairly elastic nature, and I think that it must have been understood in this way by debtors who received the respondents' letters. So far as it is used to express volition, "may" conveys the absence of a present intention certainly not the presence of one, as the majority suggests. Unlike the situations that we sometimes face where communications are hurled in staccato rhythm at partially attentive audiences of mass media, one can reasonably assume that readers of the morning mail will read and understand the common meaning of simple words. 90 F.T.C. at 388.

Commissioner Collier also stated that "there is a public interest in consumers knowing that they may be sued, and possibly assessed costs, in time to head off the consequences." 90 F.T.C. at 388. In this case as in others, when the Commission pursues unreasonable interpretations there can be a resultant loss of information that could have been beneficial to most consumers.

California Milk Producers Advisory Board, 94 F.T.C. 429 (1979). (Complaint dismissed against milk producers who had claimed that "everybody needs milk").

C.U.'s Criticism: C.U. says that the ALJ found that the ad to be unfair and deceptive because a significant portion of the population may have a so-called "lactose deficiency", and that the complaint was dismissed because the ALJ found no public interest in entering an order.

C.U. also contends that the proposed definition of deception would not affect the Commission's ability to sustain this charge in the complaint.

Response: Earlier statements about this case recognize that the ALJ agreed with the interpretation of the ads. What C.U. ignores is that the ALJ also stated that "it would be unreasonable to judge respondent's advertising to be 'unfair, false, misleading and deceptive' because of this less than 1 percent segment of the population" [that would experience symptoms from drinking 8 ounces of milk]. 94 F.T.C. at 547.

Furthermore, the ALJ found that:

[e]ven if respondent's advertising were judged from the standpoint of this small fraction of the population, however, the advertising . . . was still *not 'unfair, false, misleading and deceptive'.* The symptoms experienced by the small segment of the population are not health-threatening. The bulk of those who find the symptoms bothersome enough that they would avoid them, have learned to associate symptoms and milk drinking, and to limit their milk intake or to avoid milk. 94 F.T.C. at 547 (emphasis added).

It is difficult to imagine how these people who are allergic to milk would rely on the claim that "everybody needs milk." They would simply not interpret the ad as applying to them.

In addition, C.U. ignores the ALJ's conclusion that:

Rather than being detrimental to the health of lactose deficient persons, milk consumption provides essential nutrients not otherwise generally obtained in the absence of milk consumption. The probabilities are very high that the individuals who do not consume milk will suffer from a calcium deficiency and very likely from a deficiency of riboflavin. 94 F.T.C. at 547.

After 8 weeks of hearings involving over 12 thousand pages of testimony and 35 witnesses, the ALJ finally dismissed the California Milk complaint on a finding of a lack of public interest. The statutory standard is proposed to assure that the commission's scarce resources are not allocated to this kind of case in which the only consumers who could possibly be injured by the ad claim would not rely on that claim.

Jay Norris Corp., 91 F.T.C. 751 (1978), aff'd as modified, 598 F.2d 1244 (2d Cir. 1979) (inter alia, ads allegedly claimed socks were indestructible).

C.U.'s Criticism: C.U. challenges Chairman Miller's assertion that the "destructibility" and "everlasting" claims for nylon socks were found by the ALJ not to be deceptive and were dismissed for that reason. C.U. states that this particular charge was dismissed not because the claim was not deceptive, but because the manner in which it was deceptive, was not alleged in the complaint. C.U. also objects to any implication that the entire case was frivolous.

Response: In this case the complaint alleged the ads represented that respondent's socks are literally "indestructable" and "last forever." Reasonable consumers would not reach this interpretation. Indeed, the ALJ found that the respondent did not make those representations. Rather, the ads represent the socks are practically indestructable and that if they wear out, you would get a free replacement. Calling this replacement policy a guarantee "forever," the ALJ found there was no evidence that responsent did not live up to the guarantee "forever" implied in the claim. The ALJ did find other implied representations that were not challenged in the complaint to be false. However, he stated these were outside the scope of the complaint and that it would be unfair to amend the complaint at that time. As mentioned elsewhere, criticisms have been directed to specific claims the Commission has challenged, not necessarily to the entire case it brought. Even if only one of the claims in the case is frivolous, it wastes scarce resources to pursue it and it indicates that the Commission may go after similar claims in the future.

Bristol-Myers Co., 85 F.T.C. 688 (1975) (Dry Ban deodorant).

C.U.'s Criticism: Chairman Miller fails to disclose that the challenge to dryness claims was based on survey evidence establishing that the product characteristic in question was the one on which consumers made their purchasing decision.

C.U. agrees that challenging the dryness claim was a misallocation of FTC resources, but CU also contends that this case alone is not sufficient justification for defining deception by statute.

Response: The Bristol-Myers case is an example of the FTC's broad discretion regarding case selection. It does not stand alone; Poli-Grip [1] is another of the cases that exemplify the misuse of Commission resources to challenge claims about products that are inexpensive, frequently purchased, and easily evaluated by consumers. In these cases, deception is not a viable business strategy.

Also, Dry Ban is an example of a case in which there was no consumer injury. Consumers buying Dry Ban would have presumably purchased some other brand of deodorant anyway.

To repeat what Commissioner Thompson stated when concurring in the dismissal of the complaint:

[i]f the American consumer has no more serious problem than the possibility of being deceived as to the relative 'dryness' of his underarm deodorant, he is in much better shape than I had been led to suppose at the time I joined this agency.

Firestone Tire and Rubber Co., 81 F.T.C. 398 (1982), aff'd, 481 F.2d 246 (6th Cir. 1973) ("Safety Champion" tire name, alleged to be deceptive).

C.U.'s Criticism: Chairman Miller's criticism of this case relates to only one allegation contained in the complaint. He fails to mention that the Commission upheld the Administrative Law Judge's determination that Firestone lacked substantiation for a number of other safety-related claims concerning a line of tires.

Response: This case was cited as an instance in which the Commission staff alleged that an advertisement contained a deceptive claim that was only understood as such by a very small minority of consumers. Specifically, the Commission's complaint alleged, among other things, that the tire name "Safety Champion" implied that these tires were safer than all other tires. A consumer survey conducted by the company showed that only 1.4 percent would perceive the claim alleged in the complaint. Enactment of the proposed statutory deception standard will benefit consumers and businesses by preventing the misuse of Commission and private resources in the litigation of such unreasonable interpretations of advertising claims. The fact that in the Firestone case, the Commission complaint may have joined well-founded charges with those that were foolish, does not detract from the point.

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[1] Block Drug Co., 90 F.T.C. 893 (1977).

APPENDIX B

FEDERAL TRADE COMMISSION,
Washington, D.C., July 7, 1982.

Memorandum to: John H. Carley, General Counsel.
From: Robert J. Hughes, Attorney.
Subject: Relationship of State "Little FTC Acts" to the Federal Trade Commission Act; Impact of Proposed Amendments to § 5 FTCA on State Enforcement

I. INTRODUCTION

The purpose of this memorandum is to respond to your request for a detailed analysis of the relationship between the Federal Trade Commission Act and the "little FTC Acts" that have been enacted by the states and the impact that the amendments to § 5 of the Federal Trade Commission Act (FTCA) proposed by Chairman Miller may have upon state enforcement. The amendments referred to in this memorandum are those that would add to § 5 three elements to define unfairness and three elements to define deception as proposed by Chairman Miller in his statement to the House Subcommittee on Commerce, Transportation and Tourism, April 1, 1982.[1]

This memorandum will include the following:

A discussion of the development of state consumer protection laws (hereinafter referred to as little FTC acts for convenience), including the role played by the Commission in encouraging the states to enact uniform laws.

A classification and analysis of little FTC acts as related to the Federal Trade Commission Act, including those provisions which express legislative intent that interpretations of § 5(a)(1) FTC provide guidance in construing the state law, or otherwise indicate legislative intent that there should be consistency between state and federal enforcement.

A discussion of the growth of state and local consumer protection law enforcement programs since the 1960's.

A discussion of the amendments to § 5 of the Federal Trade Commission Act proposed by Chairman Miller and the probable impact of such amendments on enforcement of little FTC acts.

A. Development of State "Little FTC Acts"[2].—This section discusses the origin and evolution of state consumer protection laws more or less like § 5 FTC (little FTC acts) including language declaring unfair methods of competition and unfair or deceptive acts or practices to be unlawful and expressing intent that state officials and courts took to interpretations of § 5(a)(1) FTC for guidance in construing the comparable state law.

Although state laws to promote truthful advertising began to be enacted in the early 1900s (the so-called "Printer's Ink law") by the early 1960s few states had enacted any type of general law to prevent unfair or deceptive acts or practices in connection with consumer transactions. As the interest in a greater degree of protection from unfair or deceptive practices in the marketplace at the state level began to develop in the early 1960s, it became apparent that there could be considerable variation and inconsistency among the laws that might be enacted. Business firms whose operations were national or regional in scope could be faced with different standards from state to state.

With encouragement from various sources, including business organizations and members of Congress, the Commission began to encourage the states to adopt uniform or at least, consistent, consumer protection laws. An initial objective was to encourage as many states as possible to adopt the broad language of § 5(a)(1) FTCA.

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[1] The three elements to be added to defined unfairness would be (1) The consumer injury should be substantial; (2) The injury from the alleged unfair act or practice should outweigh its benefits; and (3) The harm must be one which consumers could not have reasonably avoided. The three elements to be added to define deception would be: (1) The alleged deceptive act or practice must be material; (2) A statement must be a representation of the fact, not opinion; and (3) The challenged act or practice must deceive reasonable consumers.

[2] The term "state" as used in this memorandum also includes the District of Columbia, Puerto Rico, Guam and the U.S. Virgin Islands.

In its news release of July 7, 1966, the FTC announced renewal and expansion of an earlier proposal that the states enact uniform laws to prevent unfair methods of competition and unfair or deceptive acts or practices.[3] Among the recommendations was that the following provisions be included in state consumer protection laws:

Sec. 2. Unfair competition, practices, declared unlawful: Unfair methods of competition and unfair or deceptive acts or practices in the conduct of any trade or commerce are hereby declared unlawful.

Sec. 3. Interpretation: It is the intent of the legislature that in construing Section 2 of this Act the courts will be guided by the interpretations given by the Federal Trade Commission and the federal courts to Section 5(a)(1) of the Federal Trade Commission Act (15 U.S.C. 45(a)(1)).

In recommending that states enact broad § 5 FTCA language as an alternative to more specific statutes, the Commission noted in the 1966 release that: "Another advantage of delineating the prohibited areas of conduct by use of the general terms 'unfair' or 'deceptive' is that these terms encompass all lines of business, the sale of goods as well as services, and all types of practices which may be detrimental to competition or injurious to consumers. . . ."

The following reasons were advanced for the inclusion of Section 3, the "guidance" section, in the draft.

"The Commission suggests that such legislation include declaration of intent that the State courts in construing the law be guided by the interpretations given by the Federal Trade Commission and the federal courts to Section 5(a)(1) of the Federal Trade Commission Act as has been done in Hawaii (H.R.L. Sec. 205a–1.2, approved June 6, 1965). This will give the administering official and the courts the benefits of fifty years of federal experience in the interpretation of similar language. . . ."

The Commission also recommended that:

"Exemption should be provided for acts done pursuant to regulation of the State public service commission or other regulatory body or officer acting under statutory authority of the State or United States, as in Section 19.86.170 of the Washington State law. This would avoid conflict, for example, with any 'Fair Trade Law' which the state may have adopted."

The latter recommendation was incorporated in Sec. 4 of the proposed legislation as follows:

Sec. 4. Exemptions: Nothing in this Act shall apply to actions or transactions permitted under laws administered by the State public service commission or other regulatory body or officer acting under statutory authority of this State or the United States.

At the time the 1966 proposal was released, only Washington and Hawaii has enacted similar laws.

The Commission's proposal for a uniform state consumer protection law was published in the 1967 Edition of Suggested State Legislation by the Council of State Governments and by 1969 ten states had adopted the proposal.[4] However, it became evident that alternative forms of the basic language of Section 2 of the proposal should be made available. A revision was therefore included in the 1970 Edition of Suggested State Legislation.[5]

The "interpretation" paragraph was also revised to read:

Section 3. Interpretation: (a) It is the intent of the legislature that in construing Section 2 of this Act due consideration and great weight shall be given to the interpretations of the Federal Trade Commission and the federal courts relating to Section 5(a)(1) of the Federal Trade Commission Act (15 U.S.C. 45(a)(1) as from time to time amended; and

(b) The attorney general may make rules and regulations interpreting the provisions of Section 2 of this Act. Such rules and regulations shall not be inconsistent with the rules, regulations and decisions of the Federal Trade Commission and the federal courts in interpreting the provisions of Section 5(a)(1) of the Federal Trade Commission Act (15 U.S.C. 45(a)(1)), as from time to time amended.

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[3] In 1964 the FTC proposed that the states enact a uniform false advertising law modeled after a 1963 New York law. The 1966 proposal expanded upon that earlier proposal to add the recommendation for adoption of § 5 FTCA language.

[4] Arizona, Kansas, Maryland, Massachusetts, Missouri, New Mexico, Pennsylvania, Rhode Island, Texas and Vermont.

[5] In addition to § 5(a)(1) language, the Commission advised that two alternate forms would be acceptable. The first dropped "unfair" and prohibited "false, misleading or deceptive acts or practices." The second prohibited 12 specific types of deceptive practices and added a prohibition against other false, misleading or deceptive acts or practices.

Although the Commission continued to support the enactment of the recommended provisions through the 1970s, that effort did not meet with total success as a brief summary will indicate.

(a) 21 states have adopted § 5 FTCA language declaring that unfair methods of competition and unfair or deceptive acts or practices are unlawful.[6]

(b) 8 states declare that unfair or deceptive acts or practices are unlawful.[7]

(c) 18 states declare that deceptive, fraudulent, false or misleading practices are unlawful.[8]

(d) 7 states declare that only an itemized list of deceptive, fraudulent, false or misleading acts and practices are unlawful [9] under the little FTC act [10]

(e) 24 of the states in categories (a)-(c) also include itemized lists of unfair and/or deceptive acts or practices while indicating that the lists are not inclusive but are only examples.[11]

(*Note:* Attached as Exhibit A is a table providing a current tabulation of little FTC acts including citations to the statute.)

Nor was uniformity achieved in the language of the provisions in little FTC acts providing for guidance from interpretations of § 5(a)(1) FTCA by the Commission and the federal courts or in provisions for exemption from the little FTC act for acts or practices authorized or permitted by or in compliance with the requirements of another state or federal board or agency.

The following analysis will demonstrate the variations in guidance provisions among the state statutes. (For citations and the text of the statutes, see Exhibit B attached.)

(a) Guidance: (1) The following states provide that "due consideration and great weight" or "weight" or "consideration" shall be given to interpretations of § 5(a)(1) FTCA by the Commission and the federal courts.—Alabama, Alaska, Florida, Idaho, Illinois, Maryland, Montana, Ohio and Rhode Island.

(2) The following state declares that interpretations of § 5(a)(1) by the Commission and the federal courts "may be used as a guide".—Arizona.

(3) The following states declare that the statute "shall be interpreted and construed consistently with" the interpretations of § 5(a)(1) FTCA by the Commission and the federal courts.—Georgia and Tennessee.

(4) The following state declares that the courts "to the extent possible" will be guided by interpretations of § 5(a)(1) FTCA by the Commission and the federal courts.—Texas.

(5) The following states declare their intention that the courts "be guided by" the interpretation given by the federal courts to the various statutes dealing with the same or similar matters.—Washington, West Virginia.

(6) The following states declare that the courts "will" or "shall" or "may" be guided by interpretations of § 5(a)(1) FTCA by the Commission and the federal courts.—Connecticut, Hawaii, Maine, Massachusetts, New Hampshire, New Mexico, South Carolina and Vermont.

(7) The following state declares that its statute shall be construed to make state regulation of consumer sales practices "not inconsistent with the policies of the Federal Trade Commission relating to consumer protection".—Utah.

(8) The U.S. Virgin Islands declare that "the provisions of its statute shall be construed to supplement the rules, regulations and decisions of the Federal Trade Commission and judicial interpretations of § 5(a)(1) FTCA.

(b) Exemptions: (1) In lieu of or in addition to a "guidance" provision, the following states include a statutory exemption for advertisements for acts or practices which are subject to and comply with the rules and regulations of, and the statutes administered by, the Federal Trade Commission.—Arizona, Arkansas, Delaware, Iowa, Louisiana, Missouri, New Jersey, South Carolina and Texas.

(2) The following states declare that conduct or acts or practices "regulated by or under," "in compliance with," "required by," "pursuant to," "otherwise permitted

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[6] Alaska, California, Connecticut, Florida, Hawaii, Illinois, Louisiana, Maine, Massachusetts, Montana, Nebraska, New Hampshire, North Carolina, Pennsylvania, Puerto Rico, Rhode Island, South Carolina, Vermont, Washington, West Virginia and Wisconsin.

[7] Delaware, Georgia, Maryland, Michigan, New Mexico, Ohio, Oregon and Tennessee.

[8] Alabama, Arizona, Arkansas, Guam, Idaho, Iowa, Kansas, Kentucky, Minnesota, Missouri, New Jersey, New York, North Dakota, South Dakota, Texas, Utah, Virginia and Virgin Islands.

[9] Colorado, Mississippi, Nevada, Indiana, Oklahoma, Wyoming and the District of Columbia.

[10] Total of (a) through (d) is 54 including District of Columbia, Guam, Puerto Rico and U.S. Virgin Islands.

[11] Alabama, Alaska, Arkansas, California, Georgia, Guam, Hawaii, Idaho, Kansas, Maryland, Michigan, Nebraska. New Mexico, Ohio, Oregon, Pennsylvania, Rhode Island, South Dakota, Tennessee, Texas, Utah, Virginia, Virgin Islands and West Virginia.

by" or otherwise sanctioned by another state or federal agency or law are exempt from the "little FTC act".—Alabama, Alaska, Connecticut, Delaware, Florida, Georgia, Hawaii, Illinois, Indiana, Kentucky, Massachusetts, Michigan, Minnesota, Nebraska, Nevada, New Hampshire, New Mexico, New York, Oklahoma, Oregon, Rhode Island, South Carolina, South Dakota, Tennessee, Utah, Virginia, Washington and Wyoming.

(c) Defenses: The following states declare that it shall be a defense or absolute defense in any action brought under the statute for the defendant to prove that the challenged acts or practices are subject to and comply with statutes administered by the Federal Trade Commission or rules or regulations interpreting such statute.—Idaho, New York and Ohio.

The application and interpretation of the foregoing provisions will be the subject of a detailed discussion in Section D of this memorandum. The above analysis clearly illustrates the diversity in the statutory provisions.

B. Consumer protection enforcement at the State and local level, current development.—This section discusses the growth in consumer protection enforcement resources and activities below the federal level occurring in the 1970's, the efforts of state enforcement authorities to become more productive and changes in direction at the Federal Trade Commission.

In addition to enacting consumer protection laws, the states and many local jurisdictions have allocated substantial resources to the enforcement of those laws. All 50 states, the District of Columbia, Pureto Rico, Guam and the Virgin Islands have placed the responsibility for enforcement in the attorney general's office and/or in some agency in the executive branch of state government. Even in those states where there is a non-attorney general agency with some enforcement responsibilities,[12] the attorney general may have concurrent responsibility and usually prosecutes cases presented by the non-attorney general agency.

From small budgets for most state offices in the early 1970s, the resources devoted to consumer protection enforcement at the state level increased significantly toward the end of the decade. While current budgetary constraints have affected all state programs, including consumer protection, total state funding for 1982 was still reported to be approximately $20 million. Those states with large, heavily urban populations reported the higher figures with the largest being $2,400,000 for the attorney general's consumer protection budget in Illinois. Budgets in the less densely populated Western states were lower with Wyoming reporting a budget of $50,000 for consumer protection enforcement in the attorney general office.

The $20 million total reflects the resources devoted to consumer protection activities, including enforcement of "little FTC acts." The non-attorney general agencies frequently have additional responsibilities such as enforcement of weights and measures laws, occupationallicensing laws and other functions. For those agencies, the total budgets are much higher. For example the total 1982 budget of the California Department of Consumer Affairs was reported to be $64,300,000 and the total 1982 budget for the New Jersey Division of Consumer Affairs was reported to be $5,598,000.

Attached as Exhibit C is a table showing partial data for 1973 and 1976 and complete data for 1982 enforcement budgets. The 1973 and 1976 figures were taken from incomplete tables compiled by the National Association of Attorneys General. The 1982 budget information was obtained by a telephone survey of state offices conducted in March 1982 by Federal trade Commission staff. Even though only partial data were available for the earlier years, the growth in resources devoted by the states to consumer protection activities is evident. For example, Massachusetts budgeted $303,480 in 1976 for consumer protection enforcement while the 1982 budget was $524,200 including financial aid for local enforcement. The consumer protection enforcement budget in Michigan rose from $228,000 in 1976 to approximately $500,000 in 1982. The 1976 budget in Alabama was $35,000 whereas the 1982 budget was approximately $336,000. The 1976 budget in Connecticut was $213,700 while the 1982 budget was estimated to be approximately $500,000.

Just as state governments responded to the growing demand for consumer protection in the 1970's, many city and county governments also established consumer protection offices and provided them with varying degrees of authority and resources. From a handful of local offices in the early 1970's. The total has grown to some 200.[13] The local offices range in size and resources from an office staffed with a single individual who acts as a mediation and referral office to large offices that enforce comprehensive local consumer protection ordinances.

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[12] The following states have non-attorney general agencies with a consumer protection enforcement function: California, Connecticut, Delaware, District of Columbia, Florida, Georgia, Louisiana, Minnesota, Montana, New Jersey, Nevada, South Carolina, Tennessee, Utah, Virginia and Wisconsin.

There are no available data showing the total amount of resources being devoted to consumer protection at the local level. Not even the National Association of Consumer Agency Adminstrators, which has among its members many local consumer office directors, has yet been able to compile such data. Only about 30 percent of its own members responded to a questionnaire that NACAA distributed recently. A very limited survey conducted recently by FTC staff suggests, however, that the resources may be significant. For example, the 1982 budget for the Los Angeles Department of Consumer Protection was $640,000; for the Detroit Department of Consumer Affairs, $856,000 and for the Fairfax County (Virginia) Department of Consumer Protection, $587,000. Many of the larger local agencies have additional responsibilities beyond their consumer protection activities, such as enforcement of weights and measures laws, licensing of certain businesses, regulation of cable TV and other administrative functions. Attached as Exhibit D is a table containing the results of the limited local agency survey conducted by FTC staff. Local agency budgets are also under pressure and none of the agencies contacted during that survey expected more than a cost-of-living increase in their 1983 budgets.

The Consumer Protection Subcommittee (NAAG) and NACAA, have addressed the need for state local consumers protection enforcement activities to adapt to changes in direction and emphasis taking place at the federal level. For example, at the Spring, 1982 NAAG Consumer Protection Seminar, Attorney General Bellotti of Massachusetts emphasized that it was increasingly important for the states to cooperate by exchanging information and, when possible, by filing joint lawsuits when two or more states are involved. General Bellotti cited the Northeast Regional Consumer Protection Committee as an example of this type of interstate cooperation. The Committee includes representation from New York, New Jersey, Connecticut, Rhode Island, Vermont, New Hampshire, Massachusetts and Maine. At the Spring 1982 NAAG Consumer Protection Seminar, a steering committee on state cooperative enforcement was established to develop strategies and mechanisms for interstate cooperation, including methods for determining which cases might be appropriate for joint enforcement actons. It is expected that the steering committee will report at the Fall 1982 Consumer Protection Seminar if there is no report at the Mid-Term NAAG Meeting in July 1982. Texas, Maryland, Massachusetts, North Carolina, Kansas and Iowa are represented on the steering committee. At NACAA's 1981 Annual Meeting, the central theme of the program was the need to make more productive use of local and state resources to adjust for changes in direction of the federal level.

The prompt exchange of information about interestate consumer frauds is an important element of any interstate cooperative effort and one national exchange mechanism is already in operation through the Iowa Attorney General's Office. That mechanism is the Investigation Information Exchange Project which serves as a clearinghouse for information about consumer frauds that involve, or may involve, several states.[14]

Other state attorneys general have recognized the need for the states to re-examine their role in preventing unfair and deceptive practices in the marketplace. In his remarks before the NAAG Consumer Protection Seminar in September 1981, Attorney General Tierney of Maine suggested that the states should stop relying on the federal government for guidance and the attorney general's office in each state "must become the thinkers, researchers and trend spotters." He also added that the states should shift emphasis from "chasing driveway pavers" to those areas where citizens are most affected such as health, insurance and utilites.[15]

Just as state attorneys general have recognized the need to redirect their consumer protection programs, the Commission has, since the early 1070's, increasingly focused its resources on significant regional and national matters. The growth of state and local consumer protection programs occurring in the 1970's provided adequate resources to deal with acts and practices primarily local or intrastate in character. The Commission will simply not bring that type of case today and has not for some time. While the Commission will take effective action against "hard core" consumer

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[13] Letter from Clair Villano, President, National Association of Consumer Agency Administrators, April 20, 1982.

[14] A recommendation by the FTC's Bureau of Consumer Protection that FTC regional offices and headquarters participate in the Project is in preparation and will be forwarded. Participation requires Commission approval.

[15] NAAG Consumer Protection Report, November 1981.

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fraud under an amended § 5 FTCA, those will be cases that are regional or national or national in scope and will appropriate for use of the Commission's injunctive or remedial powers in most instances.

The change in direction and emphasis at the Commission and the amendments to § 5 FTCA to incorporate statutory standards for unfairness and deception could, in the long run, complement state and local enforcement. The nature of the relationship between enforcement of the FTCA and little FTC acts and the probable impact of the proposed amendments are discussed at length in a subsequent section of this memorandum. It seems appropriate to suggest at this juncture, however, if the states choose to rely on future FTC cases and rules based on sound, empirical data, cases and rules that will prevent significant consumer injury and produce benefits to consumers that outweigh the costs of the remedy those cases and rules are likely to be of substantially greater precedential value than past FTC cases and rules perhaps not so clearly supported.

C. Proposed Changes in the FTC Act.—This section summarizes the amendments to § 5 FTCA as proposed by Chairman Miller which would incorporate standards which the Commission must meet before it may find that an act or practice is unfair or deceptive:

(1) Unfairness—The proposed amendments to § 5 FTCA which would add standards for determining whether an act or practice is unfair are taken from the letter of December 17, 1980 to Senators Ford and Danforth signed by all Commissioners and Chairman Miller's letter of March 5, 1982 to Senators Packwood and Kasten. Copies of both letters are attached as Exhibits E and F. In his statement on April 1, 1982 to the Subcommittee of Commerce, Transportation and Tourism, Committee on Energy and Commerce, House of Representatives, Chairman Miller identified the following three elements which should be added to a statutory definition of "unfairness."

(a) The consumer injury should be substantial.

(b) The injury from the alleged unfair act or practice should outweigh its benefits.

(c) The harm must be one which consumers could not reasonably have avoided.

The effect of amendments to § 5 FTCA to incorporate these three elements would be to codify the interpretation of § 5(a)(1) FTCA by the Commission as expressed in the letter of December 17, 1980 to Senators Ford and Danforth.

(2) Deception—In his statement to the House Subcommittee on Commerce, Transportation and Tourism on April 1, 1982, Chairman Miller addressed three concerns in connection with FTC actions involving deceptive acts or practices. First, the Commission is not now required to find evidence that the challenged act or practice injures consumers. Second, the Commission should only be allowed to pursue statements or representations of fact, not of opinion. Third, the Commission should measure deception by whether reasonable consumers are likely to be deceived, not whether any consumers might be deceived. With respect to his third concern, Chairman Miller commented that: ". . . This does not mean that the Commission should never protect vulnerable groups. With respect to vulnerable groups, such protection could be accomplished by focusing on whether the perpetrator knew or should have known that the act or practice was deceptive, regardless of whether or not reasonable consumers were deceived. . . ."

D. Impact of the Proposed Amendments on State Enforcement of "Little FTC Acts".—This section presents a detailed discussion of the probable impact of the proposed amendments on state enforcement of the various categories of "little FTC acts," i.e., those which have existing § 5 FTCA type language prohibiting unfair or deceptive acts or practices, those which prohibit deceptive practices generally and those which prohibit specific unfair and/or deceptive acts or practice. This section also discusses the implications of the various types of "guidance" and "exemption" provisions in little FTC acts and concludes with a discussion of relevant general principles of statutory construction.

(1) Unfairness—Of the 50 states, the District of Columbia, Guam and Puerto Rico and the U.S. Virgin Islands that have adopted some form of little FTC act, 29 jurisdictions prohibit both unfair and deceptive practices.[16] These are the jurisdictions which could be said to have some possible concern about the incorporation of the

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[16] Alaska, California, Connecticut, Delaware, Florida, Georgia, Hawaii, Illinois, Louisiana, Maine, Maryland, Massachusetts, Michigan, Montana, Nebraska, New Hampshire, New Mexico, Noth Carolina, Ohio, Oregon, Pennsylvania, Puerto Rico, Rhode Island, South Carolina, Tennessee, Vermont, Washington, West Virginia and Wisconsin.

Commission's interpretation of unfairness standards into § 5 FTCA. The other 25 jurisdictions would have no basis for concern about these amendments.[17]

Of the 29 jurisdictions that prohibit unfair practices, statutes in 19 jurisdictions provide, in varying terms, that the state courts look to interpretations of § 5(a)(1) FTCA for guidance in construing the state statute.[18] Two jurisdictions provide expressly that acts or practices which are subject to, and comply with, rules, regulations or statutes administered by the Federal Trade Commission are exempt from the state statute.[19] The remaining 8 jurisdictions which prohibit both unfair and deceptive practices do not explicitly provide for guidance from interpretations of § 5(a)(1) FTCA.[20]

There are 16 jurisdictions that expressly declare "unconsionable" acts or practices to be a violation of the state "little FTC act" including 7 that also prohibit unfair acts or practices.[21] There are also 10 states that have adopted some form of the unconscionability provision from the Uniform Consumer Credit Code which is limited in application to consumer credit transactions.[22]

Of those 8 jurisdictions which prohibit unfair and deceptive practices, but do not provide expressly for guidance to be sought from interpretations of the FTCA, the courts may nevertheless look to interpretations of § 5(a)(1) FTCA because of the similarity of the language. *North Carolina ex. rel. Rufus L. Edmisten, Attorney General* v. *J.C. Penney Company, Inc.*, 292 N.C. 311, 233 S.E.2d 895, 897 (1977); *Wisconsin* v. *Amoco Oil Company,* 97 Wis.2d 226, 293 N.W. 2d 487, 493 (1980); *Pennsylvania, by J. Shane Creamer, Attorney General* v. *Monumental Properties, Inc., et al.*, 329 A.2d 812, 817 (Supreme Court of Pa. 1974).

Irrespective of whether or not the state statute expresses legislative intent that the courts look to interpretations of § 5(a)(1) for guidance, state courts that have had occasion to consider the question have generally held that interpretations of § 5(l)(1) FTCA are not binding and that it is the state court that must determine whether the challenged acts or practices violate the state law. *Wisconsin* v. *Amoco Oil Co.*, supra; *North Carolina, ex rel. Rufus L. Edmisten, Attorney General* v. *J. C. Penney Company, Inc.*, supra at 898; *Island Tobacco Col Ltd.* v. *R. J. Reynolds Tobacco Co.*, Hawaii 627 P.2d 260, 269 (1981); *Washington* v. *Ralph Williams' Northwest Chrysler Plymouth, Inc.*, 82 Wash.2d 265, 510 P.2d. 233, 238 (1973).

As noted above, there are two jurisdictions, Delaware and Louisiana, which prohibit unfair and deceptive practices but have included a provision that acts or practices which are subject to, and comply with, rules and regulations or statutes administered by the Federal Trade Commission are exempt from the state statute. Apparently this provision has been the subject of litigation only in Louisiana. See *James F. Gour* v. *Daray Motor Co., Inc. and General Motors, Inc.*, La. App., 373 So.2d 571 (1979). In that case, General Motors argued that the challenged acts or practices (the substitution of Chevrolet engines in Oldsmobiles) were exempt because the FTC had earlier dismissed a case, In the Matter of General Motors Corp., 53 F.T.C. 1239 (1957), involving the sale of replacement parts represented to be genuine Chevrolet parts but manufactured by outside suppliers. The Louisiana Court, beginning at p. 576 of the opinion, extensively discussed the "exemption" provision and concluded that the dismissal of the earlier FTC case did not sanction the acts or practices now being challenged because the facts were significantly different.

As conceded by Assistant Attorney General John Montgomery of Massachusetts in the statement which he submitted to the Subcommittee on Commerce, Transportation and Tourism on behalf of the National Association of Attorneys General,[23] there have been relatively few reported state cases involving only unfair practices. Even one of the "unfairness" cases cited by Mr. Montgomery, *Fitzgerald* v. *Chicago Title and Trust Co., 46 Ill. App. 3d 526, 361 N.E. 2d 94 (1977), involved allegations that the challenged practice was an unfair method of competition.*

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[17] Alabama, Arizona, Arkansas, Colorado, District of Columbia, Guam, Idaho, Indiana, Iowa, Kansas, Kentucky, Minnesota, Mississippi, Missouri, Nevada, New Jersey, New York, North Dakota, Oklahoma, South Dakota, Texas, Utah, Virginia, Virgin Islands and Wyoming.

[18] Alaska, Connecticut, Florida, Georgia, Hawaii, Illinois, Maine, Maryland, Massachusetts, Montana, New Hampshire, New Mexico, Ohio, Rhode Island, South Carolina, Tennessee, Vermont, Washington, and West Virginia.

[19] Delaware and Louisiana.

[20] California, Michigan, Nebraska, North Carolina, Oregon, Pennsylvania, Puerto Rico and Wisconsin.

[21] Alabama, California*, District of Columbia, Kansas, Kentucky, Michigan*, Nebraska*, New Jersey, New Mexico*, New York, Ohio*, Texas, Utah, Virgin Islands, West Virginia* and Wisconsin*. (* Indicates that state also prohibits unfair acts or practices.)

[22] Colorado, Idaho, Indiana, Iowa, Louisiana, Maine, North Carolina, Oklahoma, South Carolina and Wyoming.

[23] Statement before Subcommittee on Commerce, Transportation and Tourism, Committee on Energy and Commerce, U.S. House of Representatives, April 1, 1982.

It would appear that the proposed amendment of § 5 FTCA to incorporate standards for determining unfairness would not inhibit state action. First, there are many acts or practices which may involve elements of unfairness but are also deceptive and could be the subject of attack on the latter ground. Second, many acts or practices which might involve elements of unfairness could be subject to attack as unconscionable in those jurisdictions which have some form of unconscionability provision, including the 7 jurisdictions with unconscionability provisions which also prohibit unfair and deceptive acts or practices.[24]

Third, recent state cases challenging acts or practice solely as being unfair may already meet the standards that would be incorporated into § 5 FTCA. See *Alaska* v. *Grogan*, Alaska, 628 P.2d 570 (1981). The Alaska Supreme Court found that defendant's acts in vandalizing the aircraft of customers who balked at paying gross overcharges constituted unfair acts under Alaska's little FTC act. The Attorney General apparently chose to proceed under the Alaska little FTC act in order to obtain restitution. Clearly, the injury was substantial, there were no benefits to consumers, and consumers could not have avoided the injury because their aircraft were in defendant's control when the unfair acts were done. Although the Court found that the acts were unfair under existing laws, there seems to be no question that the Court would have had little difficulty in finding that the acts were unfair under the standards of an amended § 5 FTCA, *if* the Court were to look to the amended § 5 FTCA or interpretations thereof for guidance. Fourth, state courts have repeatedly said that while interpretation of § 5(a)(1) FTCA may provide guidance, and may indeed be persuasive, the state courts must determine whether the state statute has been violated by the challenged acts or practices.[25] Fifth, because of the reference to "interpretations" of § 5(a)(1) FTCA in most of the state little FTC acts, until such time as cases brought by the Commission begin to work their way through the litigation process, there will be no "interpretations" that might be the subject of consideration by the state courts.

The exact meaning of the term "interpretations" has not been the subject of definition by state statute or court decision. Some statutes also refer to "rules and regulations of the Commission and statutes administered by the Commission, e.g. Ariz. Rev. Stats. § 44-1523 and Mass. Gen. Laws Anno., Ch. 93A § 2(c). Most of the statutory "guidance" provisions generally track the language suggested by the Commission in its 1966 Proposal i.e., "... the courts will be guided by interpretations given by the Federal Trade Commission and the federal courts to Section 5(a)(1) of the Federal Trade Commission Act..." In its news release of July 7, 1966 proposing the enactment of state legislation like the FTCA, the Commission noted that "... By so doing the States can draw upon the Commission's 50 years of experience and the 800 plus court decisions interpreting the Federal Trade Commission Act which declares such practices to be unlawful. . . ." It seems clear, therefore, that in adopting the "interpretations" language, state legislature intended to refer to decisions of the Commission and federal court dealing with § 5(a)(1). Only such FTC trade regulation rules as were in existence at the time of adoption would be included.

Two state courts have declined to consider FTC Guides to constitute rules or regulations or interpretations because Guides are not substantive rules which have the force of law.[26] FTC trade regulation rules clearly would be regarded as interpretations even where the state statute does not refer to rules and regulations of the Commission.

The Commission, under other state guidance proposals, included a recommended provision granting exemption from the statute for conduct "permitted under laws adminstered by a state public service commission or other regulatory body or officer acting under the authority of the state or the United States." Although 35 jurisdictions have adopted some form of that recommended exemption, there have been few reported cases involving it. The Alaska Supreme Court has held that only where a business is both regulated and unfair or deceptive acts or practices are prohibited by the regulatory agency will the exemption be granted. *Matanuska Maid, Inc.* v. *Alaska*, 620 P.2d 182, 186 (1980). An earlier reported case which squarely considered the status of the Federal Trade Commission as a "regulatory" body for the purposes of the exemption provision in a "little FTC act" is *Washington* v. *Reader's Digest Association, Inc.*, Wash. 501 P.2d 290, 303 (1972). The Supreme Court of Washington concluded that the FTC was not a regulatory body within the meaning of the exemption provision because it has no control over entry into its area of concern. According to the Court, a regulatory body must control entry and prohibit certain types of conduct.

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[24] California, Michigan, Nebraska, New Mexico, Ohio, West Virginia and Wisconsin.

[25] *Wisconsin* v. *Amoco Oil Co.*, supra; North Carolina ex rel. *Rufus L. Edmisten, Attorney General* v. *J. C. Penney Co., Inc.*, supra *Island Tobacco Co. Ltd.* v. *R. J. Reynolds Tobacco Co.*, supra; *Washington* v. *Ralph Williams' North West Chrysler Plymouth, Inc.*, supra; *Gour* v. *Daray Motor Co., Inc. and General Motors, Inc.*, supra; Arizona ex rel. *Bruce E. Babbitt, Attorney General* v. *Goodyear Tire & Rubber Co.*, Ariz. App. 626 P.2d 1115, 1118 (1981); *William J. Scott, Attorney General* v. *Association for Childbirth at Home International*, Ill. App. 407 N.E. 2d 71, 76 (1980); *Singleton* v. *Pennington*.

[26] *Wisconsin* v. *Amoco Oil Co.*, supra and Arizona ex rel. *Bruce E. Babbitt, Attorney General* v. *The Goodyear Tire & Rubber Co.*, supra.

SUMMARY OF IMPACT OF UNFAIRNESS AMENDMENTS

There are 29 jurisdictions that prohibit unfair and deceptive acts or practices.[27] Of those jurisdictions, the statutes in 19 provide, in varying terms, that the state courts look to interpretations of § 5(a)(1) FTCA for guidance in construing the comparable provision of the state statute. Eleven jurisdictions that prohibit unfair and deceptive practices also declare that a nonexclusive list of specific acts or practices are unfair or deceptive.[28]

Until such time as FTC cases brought under an amended § 5 FTCA work their way through the litigation process, there will be no interpretations which state courts might wish to look to for guidance in construing state statutes prohibiting unfair practices. Even after such interpretations become available, the impact on state enforcement would be extremely limited unless, and until, the state legislatures choose to amend the statutes prohibiting unfair acts and practices to incorporate the same elements.

Until amendment of the state statutes occurred, state courts might chose to look to interpretations of an amended § 5 FTCA for guidance but would not be bound by such future interpretations of an amended statute.

First, the provision in state statutes concerning guidance from interpretations of § 5 FTCA or providing an exemption from the statute for advertising or acts or practices permitted by or in compliance with the rules or regulations of or the statutes administered by the Commission could be held to refer only to federal interpretations of § 5 FTCA as it existed at the time of passage of the state statute. *Department of Legal Affairs* v. *Lee Roger d/b/a American Holiday Association*, 329 So. 2d 257, 267 (1976). In referring to the Florida little FTC act, which prohibits unfair or deceptive acts or practices and includes reference to "guidance from" and "consistency with" interpretations of § 5(a)(1) FTCA, the Florida Supreme Court observed in part: ". . . To preserve the constitutionality of the act, we would have to say that the legislative enactment intended only decisions made prior to its enactment (citing cases) . . . ."

Second, the state cases have made it reasonably clear that where interpretations of § 5(a)(1) as it now exists may be consulted for guidance, those interpretations are not binding. It is the state court that must decide if the state statute has been violated. Footnote 25, supra, the same view would prevail with respect to future interpretations regardless of whether the state statute has been amended.

Third, there is a substantial body of state case law interpreting and applying state consumer protection statutes which already provide "interpretations" of little FTC acts. This body of law will not disappear. While it contains few cases dealing with unfairness, the probable explanation is that the state attorneys general and private litigants have usually found other grounds upon which to challenge acts and practices that may possess elements of unfairness, e.g., the acts or practices are specifically declared unlawful by state law, the acts or practices are also deceptive; or the acts or practices are unconscionable.

Fourth, in conclusion, the 25 jurisdictions that do not prohibit unfair acts or practices would not be affected by the proposed amendments of § 5 to incorporate unfairness criteria. The potential short term impact of such proposed amendments upon the other 29 jurisdictions that do prohibit unfair acts or practices will be minimal. (See Footnote 16, supra, for a list of the 29 jurisdictions.) Unless the legislatures in those states choose to similarly amend their "little FTC acts," the long term impact

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[27] See Footnote 16, supra.

[28] Alaska, Georgia, Maryland, Michigan, Nebraska, New Mexico, Ohio, Oregon, Rhode Island, Tennessee and West Virginia.

(after interpretations of the amended § 5 FTCA are made by the Commission and the federal courts) is also likely to be minimal. This is not to say that parties under investigation or defendants in state cases will not argue that the attorney general must prove an unfairness case under the amended § 5 FTCA where the state has a guidance provision.

Ultimately, the legal effect of future interpretations of an amended § 5 FTCA containing unfairness criteria will be decided in the courts. However, the views that the proposed unfairness amendment will have a devastating effect on state enforcement and that the existing body of state and federal case law will be wiped out are not soundly based.

(2) Deception—All 54 jurisdictions prohibit deceptive or false, misleading or fradulent trade practices. In 31 of those jurisdictions the statute contains an itemized list of specific acts or practices that are declared unlawful.[29] Of those jurisdictions, 7 declare that only the enumerated acts or practices are unlawful,[30] whereas in the other 24 jurisdictions, the itemized list is declared to be non-exclusive.

In those jurisdictions where the legislature has limited violations of the little FTC act to the enumerated acts or practices, it would appear that proposed amendments to § 5 FTCA to cure the problems identified by Chairman Miller in his statement to the House Subcommittee on Commerce, Transportation and Tourism [31] would have no effect unless the legislatures of those states made corresponding amendments to the state statutes. The same argument would apply to specifically enumerated acts or practices in those jurisdictions which also provide a general prohibition against deceptive acts or practices. Nor would the proposed amendments appear to have any effect on the numerous statutes enacted by various jurisdictions which require or prohibit specific acts or practices in particular types of businesses, e.g., health spas and dance studios, business opportunity promotions, door-to-door sales, etc. even though those statutes may reference the little FTC act.

Thus, the potential impact zone for the proposed amendments that may be necessary to cure the problems enunciated by the Chairman would be in the 47 jurisdictions which have language prohibiting deceptive practices generally. But, even in those jurisdictions, the potential would be primarily limited to post-amendment efforts by the state enforcing authority to challenge acts or practices as deceptive which have not previously been declared by the legislature or the courts in those states or states with similar laws or by the FTC to be deceptive. That potential impact appears minimal.

The reasons advanced in the discussion of the potential impact of the unfairness amendments to show the limited effect on state enforcement are generally applicable to any amendments to § 5 that might be required to eliminate the problems identified by the Chairman with respect to deception.

First, until such time as the amendments are incorporated into § 5 and the Commission and the federal courts begin to construe the amended language, there will be no "interpretations" that the state courts could choose to look to for guidance.

Second, unless, and until, state legislatures choose to amend their little FTC acts to include standards for deception comparable to those that may be included in an amended § 5 FTCA, the state courts may continue to look for "guidance" to state and federal statutory and case law as it existed prior to amendments of § 5 FTCA. *Department of Legal Affairs* v. *Lee Roger d/b/a American Holiday Association*, supra. The state courts will determine whether a violation of the state statute has occurred and even interpretations of the existing § 5(a)(1), while they may be persuasive, are not binding on the state courts.[32] Third, to the extent that the amendments to § 5 FTCA to incorporate standards for deception and unfairness constituted a reduction in the reach of § 5 FTCA, there would be no conflict of a nature that might lead to possible challenges to state little FTC acts on the ground that an amended § 5 FTCA pre-empted the corresponding state statute. In passing the Federal Trade Commission Act, Congress manifested no intent to exclude states from the field of protecting their residents against unfair methods of competition or unfair or deceptive acts or practices. When Congress amended the FTCA to expand the Commission's jurisdiction to include acts or practices "affecting" interstate commerce,[33] it explicitly declared that it did not intend to exclude states from this field. The Senate Committee Report on that bill stated that it was "not intended to replace local enforcement of state or local laws against unfair trade practices." S. Rep. No. 1124, 91st Cong., 2d Sess. 9 (1970). An appropriate expression of Congressional intent in the legislative history of any amendments to § 5 FTCA could lay to rest any inferences that Congress intended to pre-empt existing little FTC acts.[34]

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[29] Alabama, Alaska, Arkansas, Arizona, Colorado, District of Columbia, Gerogia, Guam, Hawaii, Idaho, Indiana, Kansas, Maryland, Michigan, Mississippi, Nebraska, Nevada, New Mexico, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Dakota, Tennessee, Texas, Utah, Virginia, Virgin Islands, West Virginia and Wyoming.

[30] Colorado, Distirct of Columbia, Indiana, Mississippi, Navada, Oklahoma and Wyoming.

[31] The statement identified the problems as: First, the Commission currently is not required to find evidence that the challenged act or practice injures consumers. Second, the Commission should be allowed to pursue statements or representations of fact, not of opinion. Third, the Commission should measure deception by whether reasonable consumers are likely to be deceived, not by whether any consumers might be deceived.

[32] Cases cited in Footnote 25, supra.

It is well established in the law that the states may choose to provide a greater degree of protection to their residents than the FTC and that state laws or rules may be superseded only to the extent there is actual conflict with the policies or actions taken by the Commission.[35] The Commission has interpreted "conflict" to mean "inconsistent", with the latter term construed to mean that a state law that provides less protection than that afforded by a FTC trade regulation rule will be deemed "inconsistent." [36]

The statutory provisions most likely to be asserted by defendants in state actions are those that either provide a specific exemption for advertisements or for acts or practices which are subject to, and comply with, the rules or regulations of, or the statutes administered by, the Federal Trade Commission [37] or provide a general exemption for acts or practices authorized by, in compliance with, required by, permitted by federal, state or local law or regulation;[38] or provide that it is a defense to show that the challenged acts or practices are subject to and comply with the rules and regulations of, or statutes administered by, the FTC.[39] These exemption or defense provisions clearly refer only to such rules or regulations or laws as existed at the time of enactment of the state law, and would be unaffected by any amendments. See discussion of general rules of statutory construction in Section E below.

There has been little litigation involving these exemptions, but it is unlikely that these provisions would be construed to grant an exemption for advertisements or acts or practices merely because the Commission has not, by statute, order to cease or desist or rule, prohibited the challenged advertisement, act or practice. *Garland* v. *Mobil Oil Corp.*, 340 F. Supp. 1095, 1099 (N.D. Dist. Ill. 1972) (practices not within exemption for "conduct in compliance with the orders or rules of or a statute administered by a Federal * * * agency" because not mandated by federal law). While the Garland court had before it general language granting an exemption for conduct in compliance with orders or rules or statutes administered by a federal, state or local government agency [40] the reasoning of the court would apply equally to exemption provisions that specifically refer to rules or regulations of, or statutes administered by, the Commission.

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[33] Magnuson-Moss Warranty—Federal Trade Commission Improvements Act, P.L. 93-637, approved Jan. 4, 1975, 88 Stat. 2183.

[34] Congress may well be receptive to the inclusion of such an expression of legislative intent. In discussing the inclusion of unfairness criteria in § 5 FTCA, the Senate Committee on Commerce, Science and Transportation noted in its report of May 28, 1982 to accompany S. 2499, the Federal Trade Commission Amendments Act of 1982, that:

". . . The Committee knows that State Attorneys General have expressed a concern that the definition of unfairness in this section may be construed to affect provisions in State statutes or State case law.

"The Committee intends no effect whatever on those or other developments under State law. This section represents a consensus view of an appropriate codification of Federal standards, undertaken after careful assessment of the Commission's past activities. The Committee's action should not be understood as suggesting that the criteria in this section are necessarily suitable in the further development of State unfairness law or that the Commission's future construction of these criteria delimits in any way the range of State decisionmaking. Sound principles of federalism limit the impact of this section to the Commission only."

[35] *Double-Eagle Lubricants, Inc.* v. *Texas,* 248 F. Supp. 515 (N.D. Tex. 1965), appeal dismissed, 384 U.S. 434 (1966), *Mobil Oil Corp.* v. *Attorney General,* 280 N.E. 2d 406 (Mass. 1972); *State* v. *Allied Chem. & Dye Corp.*, 9 Wis, 2d 290, 101 N.W. 2d 133 (1960).

[36] Trade Regulation Rule Providing a Cooling-Off Period for Door-to-Door Sales, 16 C.F.R. 429, Note 2, Effect on State Laws and Municipal Ordinances.

[37] Arizona, Arkansas, Delaware, Iowa, Missouri, New York, South Carolina and Texas.

[38] Alabama, Alaska, Colorado, Connecticut, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Kentucky, Louisiana, Massachusetts, Montana, Nebraska, New Hampshire, New Mexico, Ohio, Oregon, Rhode Island, South Dakota, Tennessee, Texas, Utah, Virginia, Washington, West Virginia and Wyoming.

[39] Idaho, New York and Ohio.

[40] Ill. Rev. Stat., Ch. 121 § 314(1).

SUMMARY STATEMENT OF PROBABLE EFFECT OF PROPOSED DECEPTION AMENDMENTS ON STATE ENFORCEMENT

All 54 jurisdictions prohibit deceptive, fraudulent or false or misleading acts or practices. In 31 of those jurisdictions, the little FTC act also includes an itemized list of acts or practices declared to violate the statute. (See Footnote 28 above). Of the 31 jurisdictions that include itemization, seven declare that only the enumerated acts or practices are violations of the statute. (See Footnote 29 above). The other 24 jurisdictions with itemization declare that the listed acts or practices are not exclusive.

Thus, there are 47 jurisdictions that could be said to have some concern with proposed amendments to § 5 FTCA to incorporate criteria for deception. The extent of that concern would be the greatest where the jurisdiction has a guidance provision or an exemption or "defense" provision specifically referring to FTC rules, regulations or laws. Twenty-seven jurisdictions provide for guidance from interpretations of § 5(a)(1) FTCA and 9 provide for a specific exemption from the statute for acts or practices permitted by or in compliance with the rules or regulations of, or statutes administered by the FTC. (See discussion in Section A above). Three jurisdictions provide that it is a defense, or absolute defense to prove that the acts or practices challenged are permitted by or are in compliance with the rules or regulations of, or the laws administered by, the FTC. (Idaho, New York and Ohio).

In none of the jurisdictions where the statute expresses legislative intent that the courts look to interpretations of § 5(a)(1) for guidance will the administering official or the courts be bound to follow interpretations of an amended § 5 FTCA. While existing interpretations may be consulted for guidance and may be persuasive where the state law prohibits deceptive practices without defining those practices, the administering officials or courts are not bound to follow even those interpretations that existed at the time the state law was enacted. (See Footnote 25 above). Unless and until a state legislature chooses to amend its statute to conform to an amended § 5 FTCA, the administering official and the court in that state may choose not to be guided by interpretations of an amended § 5 FTCA.

In those jurisdictions where the law provides for an exemption for acts or practices permitted by or in compliance with the rules or regulations of, or the statutes administered by, FTC, it is those rules or regulations and statutes that existed at the time of enactment of the state law that would be relevant. A statutory exemption which swept in future federal rules or regulations or statutes would conflict with provisions in state constitutions. Such open-ended exemption have been deemed to be an impermissible delegation of the state legislative authority to a body outside the state. *State* v. *Rogers,* Supra; *Johnston* v. *State,* 227 Ga. 387, 181 S.E. 2d 42 (1971).

In those jurisdictions where the statute provides that it is a defense, or absolute defense, to establish that the challenged acts or practices were permitted by or in compliance with the rules or regulations of, or statutes administered by, the Federal Trade Commission such provision could be deemed to refer to those rules or regulations or statutes that existed at the time of enactment of the state law. The same reasoning would apply to defenses as to the exemptions discussed in the preceding paragraph. Of course, the consequences of changes in § 5 FTCA on state enforcement will be eventually determined by state courts analysing the intent of state legislature in enacting the little FTC act and such guidance, exemption or defense provisions as it may contain.

E. Statutory Construction: General Rules Applicable.—Under general rules of statutory construction, state courts would not be required to give weight to interpretations of language that might be added to § 5 FTCA to establish standards for unfairness or deception. As for the states whose laws specifically refer to interpretations of Section 5(a)(1) of the FTC Act, the general rule of statutory construction is that "[a] statute of specific reference [one that refers specifically to a particular statute by its title or section number] incorporates the provisions referred to from the statute as of the time of adoption without subsequent amendments, unless the legislature has expressly or by strong implication shown its intention to incorporate subsequent amendments with the statute." 2A Sutherland, Statutes and Statutory Construction, § 51.07 (Sands ed. 1973); see *Hassett* v. *Welch,* 303 U.S. 303 (1938); see also *Department of Legal Affairs* v. *Rogers,* Supra, (Florida little FTC Act, which declares a legislative intent that "due consideration and great weight * * * be given to interpretations" of the Commission and the federal courts relating to Section 5(a)(1), "incorporates" only decisions of FTC and federal courts made prior to enactment of state statute). Fourteen statutes refer to Section 5 of the FTC Act, as amended,[41] but this language has been construed as referring to amendments made to Section 5 prior to the enactment dates of the state statutes. See *State* v. *Julson*, 202 N.W. 2d 145, 151 (N.D. 1972).

Statutes of general reference, on the hand, "refer to the law of the subject generally," and "[w]hen a statute adopts the general law on a given subject, the reference is construed to mean that the law is as it reads thereafter at any given time including amendments subsequent to the time of adoption." Sutherland, supra, at § 51.07, quoting from *George Williams College* v. *Village of Williams Bay*, 242 Wis. 311, 7 N.W. 2d 891, 894 (1943). Most of the state provisions allowing defenses or exemptions for conduct authorized or permitted by federal law fall into this category but, as noted, if this defense were raised, we do not believe the state courts would hold that these provisions immunized practices simply because they were not prohibited by Section 5(a)(1) of the FTC Act.

Sutherland, supra, at § 52.02, also notes the general rule of statutory construction that "when the legislature of a state adopts a statute which is identical or similar to one in effect in another state or country, the courts of the adopting state usually adopt the construction placed on the statute in the jurisdiction where it originated." Sutherland § 52.02 continues that: The general rule also applies to make judicial and administrative interpretations of federal statutes useful in construing state statutes copies from federal acts. * * * And similarity between the underlying policies involved both state and federal antitrust laws made decisions by federal courts "persuasive" sources of guidance for interpretation of state acts. On the other hand, where state statutes have undertaken to adopt future administrative rulings under enabling legislation that was also adopted, constitutional difficulties have been encountered with reference to the delegation of legislative power to an agency that is external to the state. (Footnotes omitted).

The discussion of the issue in § 52.02 of Sutherland, supra, concludes with an excerpt from the opinion of the Second Circuit in *Iacone* v. *Cardillo*, 208 F.2d 696, 699 (CA 2nd 1953), which bears repeating, in part:

"There is a good deal of substance in the view that a legislature, in adopting a statute from another jurisdiction, is aware of, and by its acquiescence generally approves, the existing judicial construction of that statute. But this reasoning fails if applied to decisions subsequent to adoption, and, while the desire for uniformity and the respect for the ability of other tribunals in handling the same problem would seem to compel at least a respectful consideration of these later decisions, they are in no way more than persuasive, and indeed, by force of logic, may, in their conflict with legislative intent as represented by 'adoption' of the earlier decisions, be far from helpful."

F. Conclusion.—In final analysis, the proposed unfairness and deception amendments to § 5 FTCA would have a limited effect on state consumer protection laws. There will be no "devastation" and existing interpretations will not be "swept away." The states will retain the ability to protect their residents against deceptive practices in the marketplace. At worst, state court judges may employ the changes in federal law as a basis for giving less deference to those precedents called into question by Chairman Miller.

ATTACHMENTS [42]

Exhibit A—Fact Sheet on State Laws to Prevent Unfair Trade Practices.

Exhibit B—Compilation of State Laws Expressing Legislative Intent that Enforcement of State Consumer Protection Laws be Consistent With Interpretations of § 5(a)(1) FTCA.

Exhibit C—Table Containing Budget Data for State Consumer Protection Programs.

Exhibit D—Table Containing Budget Data for Selected Local Consumer Protection Enforcement Programs.

Exhibit E—Letter, December 17, 1980, to Senators Ford and Danforth signed by all Commissioners.

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[41] 1981 Al. Acts. 81-355, § 6; Conn. Gen. Stat. Ann. § 42-110b(b); Fla. Stat. Ann. § 501.204; Ga. Code Ann. § 106-1201(c); Idaho Code § 48-604; La. Rev. Stat. Ann. § 1406(4); Me. Rev. Stat. Ann. tit 5, § 207; Mass. Gen. Laws Ann. ch. 93A, § 2(b), (c); Mont; Code Ann. § 85-403; Ohio Rev. Code Ann. § 1345.02(C); R.I Gen. Laws § 6-13.1-3; S.C. Code Ann. § 39-5-20(b); Vt. Stat. Ann. tit. .9, § 2453(b); W. Va. Code § 46A-103.

[42] Attachments to this memorandum have been retained in Commerce Committee Files. Exhibits E and F are available, however, in the record of the committee's March 18-19, 1982 Hearing on Reauthorization of the Federal Trade Commission, Serial No. 97-108, pp. 23-36.

Exhibit F—Letter, March 5, 1982, to Senators Packwood and Kasten signed by Chairman Miller.

Senator CANNON. The first panel will consist of the Honorable David A. Clanton, the Honorable Patricia Bailey, and the Honorable Michael Pertschuk.

We could have let you all sit at the table at the same time because I imagine that despite your divergence of views on this, you still visit with each other.

Ms. BAILEY. Now and then.

Senator CANNON. All right, let us start off with you, Mr. Clanton.

STATEMENTS OF HON. DAVID CLANTON; HON. PATRICIA P. BAILEY; AND HON. MICHAEL PERTSCHUK, COMMISSIONERS, FEDERAL TRADE COMMISSION

Mr. CLANTON. Mr. Chairman, thank you.

I want to summarize rather briefly because I know you have a number of witnesses here today. I would like to make four basic points. First, it seems important to me that the Commission and Congress take a look at what we have done in the deception area. We have been reviewing this area for 40 years. We have literally brought hundreds of cases and have an enormous amount of experience in this area. I must say disagreements have occurred, not only in the courts but also among individual commissioners and various commissions over the past in terms of defining what constitutes deception.

Frankly, that is not surprising given the fact that reasonable people can differ in many instances over what might or might not be deceptive with respect to a particular advertisement or a particular campaign. It is also not surprising that as the courts have gained experience over time, there has been an evolution in terms of the development of the law. Likewise, I think we have become more sophisticated in our analysis.

I do think it is important that we take some effort to clarify where we are today, to try to pull together all the strands of precedent and to come up with a rather straightforward but coherent approach.

Second, having said that, I do believe, however, that the basic standards that have been set forth in the law today are valid and remain so. I think the principles of interpreting the meaning of advertisements, the principles involved in determining whether those advertisements are likely to deceive consumers and, finally, the question of whether the claims are in fact substantiated—which is an issue we do not reach in this particular set of hearings—are all standards that, by and large, looking at recent court precedent, are fairly soundly based.

I think one of the important points to remember in dealing with the question of advertising is that there is really nothing very scientific about the process of interpreting what an ad means and its likelihood of deception. It is a fairly pragmatic judgment that involves a lot of commonsense. In most instances, it involves looking at the ad itself—a very straightforward reading.

You can make a pretty reasonable determination looking at the ad. Where you cannot, it is obviously desirable, and indeed in some instances essential, to look to other evidence. That other evidence may be consumer surveys that the companies did, expert testimony, or other kinds of evidence to assist in the determination. But, by and large the process that we have to look at—the advertising copy and the media they run in—requires a very straightforward, pragmatic look at whether there is a likelihood of injury.

Frankly, that is a process that the courts can easily review. It has not forced them to become involved in very sophisticated scientific or statistical analyses, which they may get in other areas of the law. But it has given them an opportunity to look over our shoulder and secondguess us, and I must say they have in a number of instances, as to whether we have made a reasonable judgment.

Ultimately, with respect to any of the proposals that have been suggested in legislation here today, that process will not be changed. It is something that is inevitable. It is something that requires a judgmental process. For however you carve a legislative standard—whether it is the one in place today or one that may be formulated—it is going to require a fair degree of discretion on the part of the Commission and the courts to make those judgments.

I would like to quote from one of the Commission's cases back in 1963 which summarizes quite well what I think the standard of interpreting ads is today. That case says as follows:

> A representation does not become false and deceptive merely because it will be unreasonably misunderstood by an insignificant and unrepresentative segment of the class of persons to whom the representation is addressed. If, however, advertising is aimed at an especially susceptible group of people, such as children, its truthfulness must be measured by the impact it will make on them, not others to whom it is primarily directed.

I might note that that case was in 1963. It was cited with approval by the Commission in the well known *Pfizer* case in 1972. It is a principle that I think makes sense. I think it would be inevitably the kind of standard and approach that would be applied even under the various legislative proposals now pending before your committee.

I think it represents the kind of approach and policy that the Commission is applying today. Therefore, it seems to me that, on the whole, the process of ad interpretation is pretty clearly set forth in existing law and one that I do not think requires substantial clarification or modification.

My third point relates to the question of injury and how much consumer injury must be shown in deciding whether you want to challenge an ad. Again, the standard that the courts and the Commission have used in the past primarily focuses on materiality. Is the claim really central to the whole advertising theme? If it is, and it is not substantiated, then it seems reasonable to infer, as the Commission and the courts have done in the past, that consumers are likely to be misled.

No effort has been made and neither the courts nor the Commission have sanctioned efforts to go beyond that to try to survey consumers to see whether they in fact took away a misleading impression or made a wrong judgment. As a practical matter, that would really be infeasible to do and I do not think that has really been suggested.

Certainly, the chairman in his proposal does not suggest that that kind of evidence would be essential or necessary. It simply would not be feasible.

The question then is: What kind of injury? It goes back to looking at the logical consequences of a particular advertising campaign and the claims made to see whether they are directed at a particular group, whether they are central to the advertising message that is trying to be communicated, and whether they are likely to deceive consumers. If so, then it seems to me reasonable to conclude that it is something the law should take cognizance of.

Again, I think that is something that is fairly clear in existing law and has been with us for a long period of time. I would object, however, to any suggestions—and I know the chairman is not suggesting this—but with respect to any other proposals that might contemplate that we have to go further in quantifying the magnitude of injury. I think that is an appropriate thing in terms of allocating Commission resources. We have to do that all the time in making judgments. But in terms of trying to do it in litigating individual cases, I think it would simply be impractical to have to make any kind of determination as to the substantiality of harm.

That does not mean we should bring trivial cases. There certainly may be instances where there will be technically deceptive ads, especially when you get into subjective areas of taste, that may be deceptive but any consumer looking at it for more than an instant would realize that they are either being taken or there is a lot more to the issue than the advertiser has presented.

Obviously, those cases do not deserve Commission action. But where there is the potential for consumers to be put to some cost, either in purchase price or inconvenience, et cetera, then it seems reasonable to infer the liklihood of injury and not go beyond that in terms of legal analysis.

Finally, Mr. Chairman, in summing up where I stand on this legislation, I do not believe, at this time, in light of where the law is, that a change in the legal standard is called for. I do think that it would be desirable for the Commission to undertake the kind of policy statement that we did in the unfairness area, articulate and pull together these various principles of advertising deception law into a statement that would be useful not only to the Commission, to its staff, to the business community at large, but also to the Congress.

And I think it would provide you with a better basis of determining whether those standards ought to be incorporated in the law as a restatement of the law, or whether other action should be taken.

I do believe in light of what we have seen that it would be highly desirable for the Commission to undertake that process. I would have no objection if Congress directed us to do that. It could be done rather quickly. I would point out that after reading the chairman's statement today that there is a lot that I agree with. His basic approach to dealing with the question of deception I, by and large, agree with. While I might disagree on some cases, the statements of the Commissioners indicate we have gone a long way toward developing a policy statement. It probably would not take too long once we went back to the Commission to put that together. I have suggested 6 months. I think that is probably a reasonable period of time. But it is something that at a minimum we should do before further legislative action is contemplated.

Thank you.

[The statement follows:]

STATEMENT OF HON. DAVID A. CLANTON, COMMISSIONER, FEDERAL TRADE COMMISSION

Mr. Chairman and members of the Committee, I would like to thank you for the opportunity to appear today to discuss various proposals presently being considered by your Committee regarding the Federal Trade Commission's jurisdiction over deceptive acts and practices.

At the outset, let me emphasize that the dialogue initiated by Chairman Miller and others to re-examine this area is healthy and refreshing. After more than 40 years of enforcement experience and literally hundreds of deception cases, it is not too much to ask that the Commission account for what it has done and how it intends to proceed in the future. It is entirely proper, indeed desirable, to make sure that the Commission is deterring only unjustified behavior and that its policies afford reasonable guidance to business.

Thus, I believe that further inquiry is appropriate and that clarification of the Commission's enforcement policies relative to deceptive advertising would be beneficial. Having said this, however, I do not believe the evidence shows a need at this time for statutory redefinition of the Commission's charter in this area.[1] In my view, the basic legal standards are still valid; it is primarily the discretionary application of those standards that may require further refinement and clarification. At least, in the first instance, I believe that task should be entrusted to the Commission, so that a full, clear statement of the Commission's policies can be articulated, as occurred in connection with the issuance of the Commission's Policy Statement on Unfairness.[2] If that effort suggests that a statutory recodification of the Commission's power to regulate deceptive advertising is called for, there will be a much better record available for fashioning new legislation.

In reviewing the Commission's approach to deceptive advertising, there are really two fundamental issues—the identification of deceptive ad claims and the determination of the proof or substantiation that will suffice for the advertiser to avoid liability. The latter issue is important, but the sharpest controversy frequently centers on whether a particular claim has been made at all. It is the process for determining the meaning of advertisements, and the deceptive potential of the claims made therein, that is at the heart of the current debate over the Commission's authority to police deceptive marketing practices.

Under Section 5 of the FTC Act, the law is well settled that an ad is deceptive if it has the tendency or capacity to deceive consumers.[3] That standard has been criticized as being too vague and too susceptible to strained or foolish interpretations. However, properly understood, that standard simply stands for the quite reasonable proposition that an ad is deceptive if "there is a likelihood or fair probability that the reader will be misled." *FTC* v. *Sterling Drug, Inc.*, 317 F. 2d 669, 674 (2d Cir. 1963). See also *Beneficial Corp.* v. *FTC*, 542 F. 2d 611, 617 (3d Cir. 1976). In that connection, the analysis involves not only a determination as to the existence of the alleged claim but also an inquiry as to whether that claim is of a type that consumers are likely to rely upon—in other words, is the claim in theory objectively verifiable (not harmless puffery or hyperbole) and material to the purchase decision.[4]

The most difficult cases are those where the deceptive claim can be inferred only by examining the ad in its total context. In such circumstances, the law is clear that the challenged claim must be a reasonable interpretation of the advertisement. As the Commission said in a recent decision, it is not enough "that an advertisement is susceptible to every reading that it may technically support, no matter how tenuous it might be; rather the interpretation must be reasonable in light of the claims made in the advertisement, taken as a whole. . . ." The Kroger Co., No. 9102 slip op. at 9 (Sept. 25, 1981) (Citations omitted).

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[1] See also Statement of Commissioner David A. Clanton, Subcommittee on Commerce, Transportation and Tourism, Committee on Energy and Commerce, United States House of Representatives (April 1, 1982); Letter from Commissioner David. A. Clanton to Senator Slade Gorton, Committee on Commerce, Science, and Transportation, United States Senate (April 9, 1982).

[2] Federal Trade Commission Statement on the Commission's Consumer Unfairness Jurisdiction (December 17, 1980).

[3] See e.g., Chrysler Corp, v. FTC, 561 F. 2d 357, 363 (D.C. Cir. 1977).

[4] See FTC v. Colgate-Palmolive Co., 380 U.S. 374, 387, 391-92 (1965); National Commission on Egg Nutrition, 88 F.T.C. 89, 191 (1976), modified on other grounds 570 F. 2d 157 (7th Cir. 1977); Pfizer, Inc., 81 F.T.C. 23, 64 (1972).

Likewise, in an earlier case, the Commission observed that—

"A representation does not become "false and deceptive" merely because it will be unreasonably misunderstood by an insignificant and unrepresentative segment of the class of persons to whom the representation is addressed. If, however, advertising is aimed at a specially susceptible group of people (e.g., children), its truthfulness must be measured by the impact it will make on them, not others to whom it is primarily directed." H. W. Kirchner, 63 F.T.C. 1282, 1290 (1963).

I have heard the criticism that the courts defer too much to the Commission's "expertise" in interpreting ad claims. To be sure, there are numerous court decisions indicating that the Commission has reasonable latitude to determine the meaning of advertisements. But this so-called deference is often in name only. The process of interpreting ad claims is not some mystical science that only the Commission can decipher. Typically, it involves common sense judgments that the courts are in a good position to review.[5] In many instances, the task of ad interpretation begins and ends with a facial review of the ads in question. Resort to extrinsic evidence, such as consumer surveys or expert testimony, is often unnecessary if the ad, on its face, clearly makes the alleged claim. If there is ambiguity, additional evidence of consumer beliefs may be necessary;[6] however, the Commission will always consider any evidence offered by the advertiser to rebut inferences drawn from the ad itself.[7] In short, the process is a pragmatic one that is open and easily reviewable.

Any legislation that redefines the Commission's authority in this area must, by necessity, take account of the imprecise nature of ad interpretation. In fact, the pending proposals do not spell out bright line tests but, instead, attempt to circumscribe the Commission's jurisdiction by incorporating into the law some kind of reasonableness standard and/or injury determination. My concern with these approaches is that they are susceptible to varying interpretations, some of which are quite consistent with current law and policy, but also others which may go too far in preventing the Commission from taking effective action. For example, a reasonable person standard is not bad so long as it is clearly understood that consumers may react differently, but nonetheless reasonably, to particular advertising claims. If too much emphasis is placed on how a rational consumer should act, the reasonableness test is likely to depart from reality.

As for an injury criterion, that consideration is already subsumed, at least in part, by the materiality requirement. There is danger, however, that such an effort will place too much emphasis on determining the consequences of deception as distinct from its existence. If properly characterized, it seems reasonable to infer injury from a deceptive act or practice without the need to focus unduly on the magnitude of the harm. To be sure, the lack of any observable or probably injury may suggest either that the challenged claim wasn't made or that consumers didn't take it very seriously. But to have the enforcement process function efficiently, it seems to me that the law should focus on the likely interpretation and significance of advertising claims, not on the magnitude of the injury that may result from a false or unsubstantiated ad. If a claim is in fact made, and it is a central or important element of the advertising message (i.e., the claim is material to the purchasing decision), then it is reasonable to assume that injury may result. Of course, as a matter of wise resource utilization, the Commission's enforcement priorities should be directed to those areas where consumer abuse is greatest. The legal standard, however, should center on the proper detection and prevention of harmful deception.

To sum up, if the law on deception is changed, by its very nature only limited specificity can be written into the statute. Thus, a great premium will be placed on the legislative explanation or history of that change. I submit that if that task is to be undertaken, it should be done, if at all, only after there has been an opportunity for the Commission to articulate its policies in greater detail. In fact, I would have no objection if Congress or this Committee were to direct the Commission to undertake such asn effort with a view to developing a general enforcement policy, much as we did on the issue of consumer unfairness. Given the far greater precedent and rich Commission experience in the deception area, a policy statement on this subject could provide more guidance than was feasible in the unfairness area. Such a task, I would imagine could be completed within six months. Until that task is completed, I believe legislative action would be premature.

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[5] See Porter & Dietsch, 90 F.T.C. 770, 862 (1977), aff'd as modified 605 F.2d 294 (7th Cir. 1979), and cases cited therein.

[6] See Sears, Roebuck & Co., 96 F.T.C. 406, 511 (1980), aff'd 676 F.2d 385 (9th Cir. 1982); Leonard F. Porter, Inc., 88 F.T.C. 546, 625–26 (1976).

[7] The Kroger Co., supra at 10, n. 11.

[The following information was subsequently received for the record:]

FEDERAL TRADE COMMISSION,
Washington, D.C. September 23, 1982.

Hon. ROBERT W. KASTEN, Jr.,
Chairman, Committee on Commerce, Science, and Transportation,
Washington, D.C.

DEAR MR. CHAIRMAN: I am happy to respond to your questions of August 5th concerning the deception issue.

Question 1. Do you agree that the "reasonableness plus injury" test proposed by Chairman Miller should be employed as a case selection criterion? If so, why do you believe it would be so much more difficult if the agency had to convince others that it had selected its cases well? If you disagree with this test for case selection, what kinds of cases that fail to meet the test should the Commission bring? What past cases that fail this test were wise uses of the Commission's resources?

I basically agree that Chairman Miller's proposal is a good test for case selection; in fact, the Commission has been using similar criteria for some time in determining what cases are worth pursuing. As to whether the Chairman's proposal should be adopted as the legal standard for deception cases, my principal uncertainty concerns the quantum of proof that might be required. By and large, I think the Chairman's proposal is not all that different from current law, and I agree with much of the Chairman's testimony describing how his proposed standard would apply to cases previously brought by the Commission.

Nevertheless, his proposal, if enacted, presumably would increase the burden of proving deception to some extent. Just how much is not clear. But, for instance, it probably would not be sufficient to infer injury simply from the fact that the claim in issue was material to the purchasing decision. At present, materiality is the only criterion for determining probable consumer harm. It may be that the materiality test needs to be applied more carefully in the future, but it is hard for me to envision requiring much additional proof of injury beyond evidence that the claim is objectively verifiable (not purely subjective or puffery) and important to the purchase decision.

I can quite easily envisage a more rigorous test for deciding which cases to bring, since there is greater latitude at that stage to consider evidence that might be unsuited to the litigation context. But, it would be difficult, for example, to demand legal proof for all the questions posed by the Commission's 1975 policy protocol on deceptive and unsubstantiated claims.

Quite frankly, I am not sure whether the Chairman's proposal would impose unduly burdensome evidentiary standards—I agree with many of his interpretations and positions on past cases—but I feel we need to clarify the issues as much as possible before committing ourselves to a legislative redefinition. That is why I think it makes sense for the Commission to undertake a review of our deception policy to pinpoint more specifically the areas of ageement and disagreement.

Question 2. Is there a difference between "unfair" and "deceptive" advertising? Are these separable legal concepts?

With respect to the second question, I don't think there are a great many situations where an unfairness theory is the exclusive basis for challenging an advertisement. Nevertheless, I think it is stretching the deception rationale to have it reach every instance where consumers, especially children, may be unaware of the consequences of their purchase decision. I realize the deception theory has been extended to cover the failure to disclose information even though the ad in question does not affirmatively mislead consumers. Yet, I think that even a liberal application of deception law may not adequately address all instances where consumers need to be informed (through advertising) of economic or health risks. In fact, too expansive a definition of deception can undermine the concept. On the other hand, the unfairness theory is more restrictive and calls for a balancing test that makes it unlikely that advertising frequently will be found to be unfair.

I would be happy to respond to any additional questions you may have on this subject.

Sincerely,

DAVID A. CLANTON, *Commissioner.*

Senator CANNON. Thank you, Commissioner Clanton.

Commissioner Bailey.

Ms. **Bailey**. Mr. Chairman, it is really not my turn. I am lowest on the totem pole and I am unaccustomed to coming——

Senator **Cannon**. I took you out of turn on purpose. Commissioner Pertschuk has had his opportunity——

Ms. **Bailey**. You do not even want to hear from him at all?

Senator **Cannon** [continuing]. To speak at some extent——

Ms. **Bailey**. There are a lot of people who feel that way, Mr. Chairman.

Well, I cannot quote him, then.

Mr. Chairman, thank you. This is an unusual opportunity for me to come in this order. I do have written testimony that I would appreciate submitting for the record.

Senator **Cannon**. It will be made a part of the record.

Ms. **Bailey**. Thank you.

I appreciate this opportunity to testify on Chairman Miller's proposal to redefine and narrow the FTC's authority to police deceptive acts or practices in the marketplace. As you can see, the Commission, except for the chairman, opposes that initiative. Why?

As I understand Commissioner Clanton, he believes that it is not necessary at best, or at least it is premature, pending a careful jurisprudential review, to determine with clarity the current law's meaning in order to assess the potential impact on law enforcement of the chairman's proposed changes. I will not tell you what Commissioner Pertschuk is going to say. That is not fair.

I would only add a few thoughts, though. I believe he will discuss the chairman's proposal in more detail. First, there is no consensus in the law enforcement community or in the business community that the law should be changed.

True, the advertising trade associations have belatedly joined the chairman's call for a change in the deception law, but they have their own proposed language different from Chairman Miller's which I genuinely believe will paralyze enforcement and undermine and quickly eliminate the FTC's advertising substantiation program which is the basis and the underpinning of the industry's very effective self-regulation system.

That program, as you know, simply requires that before advertisers make claims in ads that they have in hand substantiation for those claims. The program is vitally important to the credibility of advertising for consumers and it protects honest competitors from the often economically severe effects of losing customers and revenues to competition who could otherwise make attractive but unsubstantiated claims for a competing product. Listerine, Mr. Chairman, was not a false advertising case but a case of advertising that was unsubstantiated.

In fact I believe the substantiation program could not be sustained under the chairman's proposal, either; but then to be fair, he has said on many occasions that he believes requiring prior substantiation for advertising claims inflicts unnecessary expense on advertisers and consumers and so should not on the whole be required.

I think that view is wrong and unwise. So do the trade associations. So, I am sure, do advertisers. In fact, as word of the ad association's enthusiasm for changing the law began to seep out from this small enclave, as Senator Ford said, however many square miles it is surrounded by sanity—I recall that from my confirmation hearings—we have begun to see expressions of alarm.

I have quoted in my written testimony from two prominent persons in the advertising industry who are appalled by the trade association's position. They represent only the tip of the iceberg, I believe. I think we could all testify to that. I, at least, have had telephone calls. I assume my colleagues have too.

Lastly, this morning for the first time we have been apprised of the actual language of the chairman's actual legislative proposal. This is on page 5 of his written testimony and he has described it verbally in these hearings. If it is enacted, the FTC could no longer find and expect a Federal court to find that an advertisement should be stopped because it had the "tendency and capacity" to deceive consumers, meaning that it was legally deceptive because it could mislead consumers and materially affect their purchasing decisions.

Instead, we would have to prove to a Federal judge's satisfaction that an ad would mislead, whatever a judge would determine that to mean, a reasonable consumer, whoever the judge determined that to be, to do something to his or perhaps her detriment, which probably means: Did a reasonable person spend more for the product than an unreasonable person would have?

It is clear that the chairman's definition, in addition to its other serious deficiencies, omits that well established deceptive practice of omitting material facts. I can give you two concrete examples of what that means. When a land sales company offers land for sale in Florida, describing it accurately with trees and grass and an ocean view, but omits to say that it is under water, that is deceptive, I think. At least the courts have said so.

For cigarette companies to advertise their cigarettes without giving a health warning is to omit a material fact. That is missing from the chairman's proposal.

Lastly, the chairman's proposal and all other proposals to change the law will have a direct impact on State law. The National Association of Attorneys General will testify later about that in these hearings.

The chairman has argued that a change in the national law against deceptive trade practices will not affect the laws of the 49 States that have little FTC acts modeled directly on our statute. I believe he is wrong. But the problem is this: If he is wrong, then law enforcement at the State level will be seriously disrupted and confused.

If he is right, then advertisers and their ad agencies will be subjected for years to the uncertainty of a new national standard plus 49 different State standards as the States could be expected to continue enforcement of their own laws by relying on well-established but now in doubt precedent of 44 years.

Thank you, Mr. Chairman.

[The statement follows:]

STATEMENT OF HON. PATRICIA P. BAILEY, COMMISSIONER, FEDERAL TRADE COMMISSION

Mr. Chairman and members of the Committee, I am pleased to have the opportunity to testify here today along with my fellow Commissioners about proposals which have been made in recent months to redefine and narrow the Federal Trade Commission's jurisdiction over deceptive trade practices. As you know, I, together with Commissioners Clanton and Pertschuk, oppose proposals to alter the "deception" standard of Section 5 of the FTC Act and I appreciate this opportunity to explain my views more fully.

All of the proposals which have been advanced so far to alter the statute's language would substantially narrow the FTC's authority over deceptive practices. I oppose them because I am unaware of any sustained criticism of the Commission's exercise of its deception jurisdiction by the business or advertising communities. Those who live with the standards of conduct the agency has developed over the years appear to understand well both the law's parameters and the agency's procedures for enforcing it. My observation is that the system works and works effectively for all concerned. Also, I believe considerable legal mischief would ensue should any change be made, no matter its purpose or intent. Prevention of deceptive practices would inevitably be made more difficult, time-consuming and costly at a time when shrinking budgets demand the opposite.

To understand the potential impact of each of the proposals to redefine deception, it is necessary to analyze critically what such changes would mean to 44 years of precedent defining the agency's and the states' authority to proscribe deceptive practices and therefore how the proposals would affect future federal and state enforcement in this area.

I mention state enforcement because one important aspect of any revision to Section 5 which cannot be overlooked is the impact it would have on state law enforcement. Any changes to Section 5 of the Federal Trade Commission Act could also affect the laws in many states which have adopted "little FTC Acts" modeled on the federal law. Forty-nine states and the District of Columbia have enacted statutes more or less like the FTC's to prevent deceptive and unfair trade practices. In many of the states, these "little FTC Acts" track the FTC Act's exact language, and several states either by statute or court decision also provide that Commission cases shall be used in interpreting the scope of state law.[1] It is clear, then, that the states would be affected by any limitation of the FTC's authority to police deceptive practices, and to the degree that confusion and uncertainly over the scope of our jurisdiction followed such a change, the same confusion and uncertainly would also be introduced into state enforcement activities. I believe that the Committee is scheduled to receive testimony on this subject later in these hearings from the National Association of Attorneys General.

The FTC Act has prohibited "deceptive acts or practices" since 1938, and during the ensuing 44 years there have been hundreds of administrative and judicial decisions construing that term. Even before the 1938 Wheeler Lea Amendments added jurisdiction over deceptive practices to the FTC Act, a large body of common law had developed the concept of false, deceptive or misleading trade practices. Since 1938, cases brought under the UCC and other state laws have continued to amplify on these concepts and on the principle that fraud in the inducement of a contract, through misleading representations or material omissions of fact, is illegal.

A large body of case law has developed in this way, and there is little evidence that I am aware of that thee authority to prohibit deceptive practices has been used by the FTC, (or the states or private litigants for that matter) in a manner that has consistently injured consumers or businesses—except, of course, for those businesses that have engaged in deceptive practices. Without some substantial indication of what types of worthwhile business practices are supposedly being stifled by the application of the current statutory definition, Congress is being asked to remedy a "problem" which cannot be demonstrated to exist.

As the Committee is aware, it is no trivial matter to alter 44 years of jurisprudence. If the prohibition on "deceptive practices" is altered, no matter how benign the intentions of those making the change, the natural assumption of the legal community, including state and federal judges, will be that Congress intended to change the actual effect of the law. The inevitable result will be that at least some deceptive practices which are now illegal under current law will become legal, as judges and lawyers are cast adrift from precedent to search for the new law's meaning. Only one thing is certain—any change will be a bonanza for lawyers. With 44 years of legal doctrine in doubt, every new FTC case will have to be decided in an atmosphere of uncertainty concerning the applicability, if any, of established precedent.

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[1] See, e.g., statutes in Illinois, Ill. Ann. Stats. Ch. 121-1/2 § 262 (Smith-Hurd 1960 & Supp. 1981); Washington, Wash. Rev. Code Ann. § 19.86.020, .920 (1978 & Supp. 1981); Massachusetts, Mass. Gen. Laws Ann. Ch. 93A § 2 (West 1972 & Supp. 1981); Maryland, Md. Com. Law Code Ann. §§ 13-105, 13-301, 13-303 (1975 & Supp. 1981); Maine, Me. Rev. Stat. Ann. title 5 § 207 (1979 & Supp. 1981); and New York, N.Y. Gen. Bus. Law § 349 (McKinney Supp. 1981).

Following a change in the statute, the first step for lawyers representing a company which has been sued by the FTC for engaging in "deceptive practices", would be to ask the agency or the federal courts to reconsider the action, and determine first whether the lawsuit could be justified under the new statutory standard. Added litigation and delay in the work of the Commission and the courts is virtually certain. Further, any change could cast into doubt the validity of hundreds of cease and desist orders issued in accordance with past precedent. It is fully predictable that the agency would be flooded with requests to reopen and reconsider all orders issued over the past four decades. This kind of administrative nightmare could also occur on the state level, particularly in states which pattern enforcement on FTC precedent.

Before turning to an analysis of the specific proposals which have been offered thusfar, there is one additional general observation that I would like to share with the Committee. Over the past two or three months since these proposals have been advocated seriously before the Congress, I have had many opportunities to discuss them with Members of Congress and their staffs, the business community, the private bar, consumer organizations, state attorneys general and representatives of the media. On each of these occasions. I have been struck by the fluid and confusing nature of the proposals. Most of those with whom I have spoken cannot agree on the correct interpretation of each proposal or how any or all of them would operate. Indeed, it has often happened that as soon as they have finished debating one proposal, another, completely different suggestion is advance.

For example, after initially advocating one approach before this Committee last March, it is my understanding that the Chamber of Commerce and the National Association of Manufacturers now advocate a different approach. In addition, representatives of three advertising trade associations, who earlier did not support proposals to redefine deception before this Committee, later testified before the House Subcommittee on Commerce, Transportation and Tourism that they supported Chairman Miller's desire to modify the law, but had different language to propose. Finally, the Committee has before it Chairman Miller's proposal. To my knowledge, however, the Chairman has not yet suggested the actual legislative language he would use to accomplish the modifications he proposes and I have heard several different interpretations of how such language would both read and operate.

Faced with what can only be described as a moving target, the constituencies interested in the subject of the FTC's deception authority have responded in a variety of ways. As mentioned above, the state attorneys general have expressed alarm over the proposals and urged the Congress to consult with them further before any step is taken to amend the statute. Consumer groups perceive these changes as an assault on the FTC's consumer poptection mandate and have responded to that effect. The most recent reaction has come from within the business community, and I believe it should not be ignored. As word of the various proposals becomes more widespread, additional individual reactions from affected businesses can be expected.

In a recent speech to the American Advertising Federation's 1982 national convention, David McCall, Chairman of the Board of McCaffrey and McCall, Inc., said to his fellow advertisers:

"I stand before you as someone whose agency and clients have been stung more than once by the Federal Trade Commission. I have considered them to be arbitrary and unfair on occasion. I, in a flight of rhetoric, even likened their young lawyers to the Baader-Meinhof gang. So, I am not a wooly-head who has no sympathy with the annoyance that people feel for the FTC.

"However, the Federal Trade Commission is in place for a purpose. And, it is an important one. It is to protect the American consumer against the actions of unscrupulous businessmen. In protecting the American consumer against dishonest practice, it is, of course, protecting the honest businessman—the vast majority—against the activities of the unscrupulous businessmen, who are few but dangerous. You can't compete fairly with a crook whose methods and practices are not governed by a reasonable code of ethics.

"That is the reason why the Federal Trade Commission has asked for substantiation of claims made on behalf of products. That's why the Federal Trade Commission has said that advertising should not be deceptive or unfair. . . .

"[Now] . . . both of these pillars of public protection have been attacked, and I have found it disappointing to see some of the leaders of the advertising business in full support of Chairman Miller's comments, when even his fellow Republican Commission members were not in agreement. . . .

"[Our business must hew to the principle of judging each issue by its impact on the welfare of the public as well as its impact on business.

"Substantiation of claims and a reasonable demand for fairness in advertising are in the interest of the public and in the interest of legitimate business. I am not the only advertising practitioner who would perfer to see our associations stand in back of these important contributors to a strong Federal Trade Commission."

In response to these remarks, Ronald J. Moss, vice president of Kenyon and Eckhardt, wrote Mr. McCall a letter expressing support for his views on the FTC. Mr. Moss has been kind enough to provide me with a copy of that letter. Among other things, he said:

"Our colleagues in the agency business have short memories. When I started as general counsel to Kenyon and Eckhardt in the sixties, every vigilante with a few dollars and a postal meter could start an avalanche of adverse publicity about an ad or commercial. They did so knowing that with any luck at all, they would become the darlings of some media (preferably the nightly network news, New York Times or Washington Post). Typical of those groups, the attacks were often vicious, subjective and usually grossly unfair.

"Eventually, the FTC regained its vigor . . . and while I agree with your suggestion that a few of the FTC lawyers were Kamikaze pilots at heart, things finally sorted themselves out and sanity or near sanity emerged. Now our brethren smell an easy victroy over a shell-shocked FTC. Budget constraints have already severely limited its ability to do its job.

"What I think our colleagues fail to grasp is that the media will quickly seize an old opportunity and begin once again to legitimize every crackpot 'environmentalist-consumerist' with an axe to grind. Heaven help us!"

Mr. McCall and Mr. Moss are both addressing, in different ways, the perception that could be created if the Congress adopts any of the various proposals to redefine and narrow the FTC's deception authority. I find their predictions particularly interesting because they have both been highly successful in a profession devoted to the creation of clear public images or perceptions of given products and services. Beyond the specifics of their viewpoints, the very fact that both chose to speak out on these issues illustrates the absence of any firm consensus among the business community concerning the need for, much less the details of, any statutory change. I hope that this Committee will take the opportunity to explore further these differing views.

Turning to the various proposals, I am aware of three separate propositions contained in them. The first, incorporated in S. 1984 (introduced by Senators McClure and Melcher) and advocated by the Chamber of Commerce, the NAM and the advertising trade associations, would require the Commission to go beyond proving that a sales claim was false or misleading, and also prove that the ad caused substantial consumer injury which can be quantified. Under S. 1984 and the Chamber/NAM proposal, the Commission would further be required to prove that the benefits of halting such injury do not outweigh the costs to business of ceasing its deceptive activities or claims, or, that is to say, that there are not countervailing benefits (which accrue from the deceptive practice) which outweigh the consumer injury caused by it.

The second modification, also incorporated into the proposals made by the Chamber, NAM and the advertising trade associations, would allow the FTC only to prosecute claims which consist of misrepresentations "known to be false or made in reckless disregard of their truth or falsity."

A third approach, suggested by Chairman Miller, would (1) require a finding that the challenged act or practices was "material" as that term is understood in the common law; (2) exempt statements of opinion; and (3) limit deception to situations where "reasonable" consumers are likely to be deceived, except in cases where vulnerable groups of consumers are involved and the company knew or should have known a practice was deceptive.

ACTUAL INJURY AND BENEFIT/COST PROOF REQUIREMENTS

The bill introduced by Senators McClure and Melcher, S. 1984, would require a showing that a deceptive act or practice "causes substantial consumer injury that outweighs the benefits derived from such act." The Chamber of Commerce and NAM have proposed to amend Section 5 to prohibit ". . . deceptive acts or practices . . . where such acts or practices directly cause or may foreseeably result in substantial injury to consumers and such injury is neither reasonably avoidable by consumers themselves nor outweighed by countervailing benefits to consumers or competition . . .".[2] The advertising trade associations have proposed instead that deceptive acts or practices should be declared unlawful where they "consist of misrepresentations that directly cause or may foreseeably result in substantial injury to consumers acting reasonably in the circumstances."

These proposals appear similar in intent—i.e., to require that the Commission find that costs outweigh benefits before prohibiting deception under Section 5. However, since the Chamber, NAM and the advertisers have discussed in some detail how they intend such a provision to operate, I will focus my comments on their statements. I would note, though, that the kind of approach taken in S. 1984 could easily pose the same problems for future Section 5 enforcement that I identify below.

The Chamber of Commerce and NAM have charged that in applying its authority to proscribe deceptive acts or practices, the Commission has ignored the "requirement" intended by the Congress that it prove consumers suffered "actual injury" as a result of the deceptive practice. The Chamber and NAM explain that proof of "actual injury" means proof that consumers would have made a different purchasing decision but for the deceptive misrepresentation. They have criticized a long line of Commission cases, upheld by several federal circuit courts, which stand for the principle that the Commission need not probe the minds of all those who heard the deceptive statement to determine whether they would have bought the product without it; rather, the Commission need only show that the statement has the "tendency and capacity to deceive" consumers. Their proposal appears to be designed to reverse this doctine and to require instead that the Commission prove a direct causal link between the deceptive representation and substantial, "actual" consumer injury.

The Chamber asserts that its proposal would not impair the Commission's ability to condemn and prevent "actual" deception. It says that falsehoods and "intentionally misleading" representations have no proper place in a well-functioning free market and that "by their very nature" such "fraudulent" behavior is "intended to inflict and does inflict substantial injury on consumers." Because such conduct "has no redeeming virtue and cannot reasonably be avoided," Commission enforcement actions against such acts or practices could continue under the Chamber/NAM proposal.[3]

Despite the Chamber's contention that law enforcement efforts against "actual" deception could continue uninterrupted, it is clear that both the Chamber and NAM intend their proposals to change dramatically the burden of proof the Commission must assume to prove even a false (much less a misleading, or unsubstantiated) advertising case:

"[The proposal] would require the Commission to take questionable consumer practice one step beyond the intuitive finding that conduct may potentially or even actually result in consumer injury. The Commission would be required to show, on the record, that the actual injury at issue could reasonably have been foreseen. Thus, the Commission must clearly prove that enough information exists by which the Commission can draw the conclusion that absent federal intervention injury is not only likely to occur, but is foreseeable under the circumstances." (Emphasis added.)[4]

Perhaps the most helpful way to illustrate how the Chamber/NAM proposal could operate in practice is to review how it would change the prosecution of one of the Commission's best-known false advertising cases—the case involving Listerine mouthwash.[5]

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[2] The Commission itself, in December 1980, formulated the "substantial injury/not reasonably avoidable/not outweighed by countervailing benefits" standards in explaining the exercise of its authority to proscribe unfair trade practices. These standards were derived from an analysis of all prior unfairness cases. That analysis took several months and involved a painstaking effort both to describe the development of unfairness law and to distinguish it from the development of deception law. Any effort to apply the unfairness standards to the Commission's deception authority ignores the separate development of these two doctrines and it would be done without the benefit of an in-depth analysis of how the deception doctrine has evolved over 44 years in both federal and state caselaw. (See Letter from Federal Trade Commissioners to Senators Wendell H. Ford and John C. Danforth (December 17, 1980). See also the Commission's opinion in the matter of Horizon Corporation, 97 F.T.C. 799, 847 (1981), which incorporated the standards stated in the letter.)

[3] Statement of the Chamber of Commerce (at page 28) before the Subcommittee on the Consumer of the Commerce, Science, and Transportation Committee, United States Senate (March 19, 1982).

[4] Statement of James F. Carty on Behalf of the National Association of Manufacturers (at page 9) before the Subcommittee on the Consumer of the Committee on Commerce, Science, and Transportation, United States Senate (March 18, 1982).

[5] *Warner-Lambert Company* v. *FTC*, 562 F.2d 749 (D.C. Cir., 1977).

That case challenged the claim that Listerine could "cure" or "prevent" colds, which was one of several claims included in a typical advertisement for the product. The Commission proved to the satisfaction of the circuit court of appeals that there probably is no "cure" for the common cold and that, in any event, Listerine was not such a cure. Satisfied by this fundamental finding of false advertising, the court upheld the Commission's order barring future misrepresentations and requiring corrective advertising to reverse the general misimpression in the minds of the American public that gargling with Listerine every morning would prevent colds and sore throats.

Under the Chamber/NAM and advertisers' proposals, future Listerine cases could not be considered in nearly such a straightforward manner. In fact, as I read the proposal, the Commission could be forced to jump through the following procedural hoops in order to find the same violation of Section 5:

First, we would have to conduct a statistically valid survey to prove that a substantial number of the consumers who bought the mouthwash after seeing the ad did so because they thought it would cure colds and *not* for any other reason. It would not be enough for us to draw the common sense inference that this central claim probably caused consumers to purchase the product; instead, we would have to prove a direct causal link between the claim and their behavior.

Second, once we had proven that a substantial number of people bought the product only because they thought it would cure colds, we would then have to explore whether consumers could have avoided any injury caused by their purchase of the product. Could they, and if so, how long would it take for them to discover that repeated applications of the mouthwash did not dispose of their colds?

Once we had assembled empirical evidence to show that consumers could not discover Listerine's failings for themselves—by proving through expert testimony, for example, that all colds go away sooner or later anyway and so it is hard to tell whether time or mouthwash "cures" them—we would then have to explore exactly what kind of injury consumers suffered when they bought the product. Did they pay more for Listerine than they would have otherwise had they not been subjected to the deceptive claim? Even if they did, could the Listerine have helped ease their cold symptoms more than other products and was the additional relief worth the extra money? What was the alternative to Listerine? Another, cheaper mouthwash which was not as good? Or no mouthwash at all? What are the health or cosmetic benefits of using a mouthwash? What if consumers hadn't bought Listerine or any other mouthwash but instead had realized they needed to buy a completely different kind of symptom reliever? Would those other products have been effective? Answers to all of these questions and possibly other could be necessary to demonstrate and quantify the "actual" injury caused by the concededly false advertisement.

Finally, under the Chamber/NAM proposal we would have to show that this injury was "reasonably foreseeable" by Listerine. In the original case, the company had some inadequate studies showing that Listerine might help ease the symptoms of a cold. Would these studies immunize its false advertising from an FTC "cease and desist" order? Why should intent be an element of proof when the remedy for the practice is not criminal but merely a prospective order prohibiting its repetition?

The preparation of the kind of case I have outlined above would be very costly not only for the Commission but also for the respondent company. The higher the FTC's burden of proof, the more information we would have to obtain by compulsory process from the target of an investigation. We would undoubtedly bring far fewer cases, but the targets of those we did bring might soon wish the definition of deception had never been changed.

In addition to severely complicating the prosecution of a straight falsity case, the revised standards of proof could also have the effect of eliminating the Commission's advertising substantiation program because it might be almost impossible for us to establish a causal link between the lack of substantiation and consumer behavior. The purpose of the ad substantiation program is to encourage advertisers to have support for the claims they make before disseminating commercial messages. Under the Chamber/NAM and advertisers' proposals, we might have to prove that had consumers known a specific claim could not be substantiated, they would have changed their purchasing behavior. We might also have to prove that the claim was in fact false since otherwise it would probably be argued that consumers suffered no injury from relying on it.

In sum, the Chamber of Commerce, NAM and advertisers' proposals could require the Commission and the states to carry a well-nigh impossible burden of proof by having to demonstrate that the majority of those exposed to a deceptive claim would have made a different purchasing decision but for the deception.[6] The propoals threaten continuation of the Commission's advertising substantiation program, which is the basis for an extensive network of industry self-regulatory mechanisms. And finally, they would cast doubt on 44 years of precedent and severely complicate the Commission's efforts to exercise its authority to proscribe deceptive acts or practices for many years to come.

PROOF REQUIREMENTS CONCERNING INTENT TO DECEIVE OR RECKLESS DISREGARD OF TRUTH OR FALSITY

The advertising agencies have proposed that a two-prong test be enacted to define deception. The first, "misrepresentations that directly cause or may foreseeably result in substantial injury to" reasonable consumers is discussed in the foregoing section. The second prong of their test would allow the Commission to prosecute deceptive acts which consist of material representations known to be false or make in reckless disregard to their truth or falsity.

The trade associations stated in their testimony before the House of Representatives that "any definition should require advertisers to act responsibly and should reinforce the requirement for bona fide ad substantiation." [7] I sincerely doubt whether either of these laudable goals could be met if the Congress adopts the changes they advocate.

Advertising trade association representatives have said to me that the "intent to deceive/recklessness" standard they propose—as opposed to the "substantial injury" prong of their two-part test—would be the standard governing ad substantiation cases. Although the advertisers believe that the substantiation program, and other cases challenging deceptive advertising, could continue under this "recklessness" standard, it is far from clear that the Commission could pursue a credible law enforcement program should it be enacted into law. "Recklessness" is an extremely high legal standard, never before a part of the law governing advertising. To apply it in this area, the courts will turn to the case law of libel and torts, from which the standard is directly derived.

In the well-known cases of *New York Times Co.* v. *Sullivan,* 376 U.S. 254 (1964) and *Time, Inc.* v. *Hill,* 385 U.S. 374 (1966), the Supreme Court articulated the standard for libel concerning matters of "public interest" as "proof that the defendant published the report with knowledge of its falsity or in reckless disregard of the truth." The Supreme Court has consistently emphasized that such a high standard for libel in cases involving public officials or matters of public interest is necessary in order to safeguard First Amendment guarantees of free speech and a free press. It is probably unnecessary to point out what is generally conceded: given the "reckless disregard" standard and the virtual impossibility of proving it, public officials and public figures cannot hope to win a libel case except perhaps in the grossest kind of circumstances.

Commercial speech, on the other hand, was not held by the courts to be entitled to basic First Amendment protections until the mid-1970's. The Supreme Court's most recent exploration of the constitutional protections to which commercial speech is entitled is *Central Hudson Gas & Electric Corp.* v. *Public Service Commission of New York,* 447 U.S. 557 (1980), where the Court held that a three-part balancing test should be applied in deciding whether an infringement on commercial speech is constitutional: (1) the speech must concern lawful activity and not be misleading; (2) it must be determined whether the asserted governmental interest to be served by the restriction on commercial speech is substantial; and (3) if both inquiries yield positive answers, it must then be decided whether the restriction directly advances the governmental interest asserted and whether it is the least drastic alternative available.

Thus, it is clear that the recklessness standard for libel concerning matters of public interest and the Central Hudson three-part test stand at opposite ends of the spectrum of constitutional protections afforded these very different types of speech. The advertisers ask the Congress to cut the FTC's ability to police deceptive advertising back to the libel standard. Such a change would mean that consumers would have no more protection from deceptive advertising than public figures have from free-wheeling (and often false or totally unfounded and damaging) press commentary about them.

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[6] In the case of advertising in the mass media, the Commission would presumably have to track down not only those who saw the ad, but also those who subsequently bought the product.

[7] Joint Statement of the American Advertising Federation, the American Association of Advertising Agencies and the Association of National Advertisers Proposing and Supporting Amendments to the Federal Trade Commission Act (at page 9) before the Subcommittee on Commerce, Transportation, and Tourism of the Committee on Energy and Commerce, United States House of Representatives (April 1, 1982).

The second place to look for the legal meaning of "recklessness" is tort law. The term "recklessness" is applied there to actions of gross negligence and has been described as one of "quasi-intent". In the state of Washington, to take one example, the courts have held that a person who drove at 50–60 miles per hour without slowing down between a row of parked cars and a truck, all of which were standing with their headlights on and so close together so that there was barely enough room to pass, and struck a pedestrian, was behaving recklessly. *Liebhart* v. *Calahan,* 434 P. 2d 605 (Wash. 1967). It is difficult to imagine what kind of dramatically irresponsible conduct an advertiser would have to engage in before its actions reached an analogous level of recklessness. I think we can predict some decidedly bizarre results should the courts ever have occasion to apply the tort standard in FTC advertising cases.

Finally, I would point out that all of these proposals and the discussion about them ignores the highly significant point that "deceptive trade practices" is a far wider category than just advertising. To my knowledge, neither Chairman Miller nor the ad associations have addressed the potential impact of their proposals on the myriad of deceptive practices challenged by the Commission and the strates over the years which have nothing to do with advertising. For that reason alone the Congress should hesitate to alter this statutory standard pending at least a review of the impact of a new statute outside the world of Madison Avenue.

CHAIRMAN MILLER'S PROPOSALS TO REDEFINE DECEPTION

Chairman Miller has proposed to redefine deception by incorporating a "materiality" element, exempting statements of opinion and limiting the agency's jurisdiction to practices which would deceive only "reasonable" consumers, except in those cases involving practices aimed at vulnerable groups where instead of having to demonstrate "reasonableness" on the part of members of vulnerable groups, the Commission could show the proposed respondent "knew or should have known" the practice was deceptive.

A "material" misrepresentation, under the common law, is a misrepresentation on which consumers are likely to rely to their detriment in making a marketplace decision. The Commission and the federal courts have already construed Section 5 to apply only to "material" misrepresentations.[8] However, the Courts have recognized that the Commission may resonably infer that a deceptive statement would materially affect consumers' marketplace decisions without requiring the Commission to conduct an expensive survey of actual consumer behavior. If addition of an express "materiality" standard to the FTC Act would mean imposing this type of proof requirement before the Commission can prohibit a demonstrably deceptive practice, the Commission will find it prohibitively expensive to pursue many cases of false advertising in the marketplace for the same reasons noted in my comments on the Chamber/NAM proposal. If the Chairman's change is not designed to eliminate the Commission's authority to infer materiality, then the change is unnecessary. Unfortunately—or fortunately—however, courts do not assume that Congress legislates for no purpose and so any change is likely to invite litigants and judges to read in the proof requirement noted above.

As for the second change, limiting deception to statements of "fact," not "opinion," I would observe that existing law already makes that distinction to the extent it is desirable, and the proposed modification is likely at best to sow confusion and at worst to provide a refuge for future false advertising.

The FTC and the courts have long recognized that "mere puffery" is not actionable by our agency. If a claim is not objectively verifiable, and is by its nature a matter of opinion, an advertiser cannot be sued for making it. For example, the statement "our cookies taste best" is clearly puffery. So is "our gasoline puts a tiger in your tank" or "Coke is the real thing." On the other hand, the statement "you can earn $100,000 a year as our franchisee" is a statement that can be verified by experience and supported by analysis, and an advertiser will be held liable for its accuracy and supportability.

Explicitly limiting the ban on "deception" to statements of "fact" invites the unscrupulous to dress up misleading statements in the guise of opinion, in order to take advantage of the express exemption granted opinion statements.[9]

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[8] *FTC* v. *Colgate-Palmolive,* 380 U.S. 374, 392 (1965).

[9] If the Chairman's standard is meant to turn on "substance" rather than "form" (i.e. whether consumers actually understand a statement to be one of opinion or one of fact, regardless of

Continued

The third proposed change would inject a requirement that consumers behave "reasonably" before they are entitled to protection by the FTC. For vulnerable groups like children or the elderly, the Commission would have to show that a company "knew or should have known" the practice was deceptive.

As the law now stands it protects against any claims likely to deceive a substantial number of citizens. No inquiry is required to determine whether the conduct of those fooled meets some undefined standard of "reasonableness." In pracitce, of course, the Commission would not pursue a case involving conduct that would be likely only to fool someone behaving capriciously. The difficulty with the proposed change is that it could be read as a direct repudiation of the existing judicial standard, which was designed to protect the average consumer from deception.

Take, for example, the following quotation from a 1942 case involving the sale of a product called "Triple X Compound", which had been advertised as a cure for delayed menstruation in women. The product was both ineffective and dangerous. The advertiser argued that its artfully worded advertisements did not literally claim the product would be effective and that consumers (especially reasonable ones, presumably) should have understood the literal meaning of the ad. In rejecting this argument, the seventh circuit Court of Appeals wrote:

"The law is not made for experts but to protect the public—that vast multitude which includes the ignorant, the unthinking, and the credulous, who, in making purchases, do not stop to analyze but too often are governed by appearances and general impressions. . . . Advertisements are intended not to be carefully dissected with a dictionary at hand, but rather to produce an impression upon prospective purchasers." *Aronberg* v. *FTC,* 132 F.2d 165, 167 (7th Cir. 1942).

Would this case be overruled by a reasonableness requirement? Perhaps that is not the intent of the proposal but it is by no means certain what kinds of consumer behavior could be labeled "unreasonable" by the courts. To cite just a couple of examples: is it "reasonable" to buy undeveloped land sight unseen? Tens of thousands of consumers have done so and, where the Commission found the sales pitch they were given was deceptive, we have obtained redress for them. Is it reasonable to permit yourself to be baited and switched to a more expensive product than you went to a store to buy? You are always free to leave the store and I can easily envision a court holding that "reasonable" consumers would have avoided being deceived by this practice which is routinely held to be deceptive.

As for the suggestion that the Commission prove that a company "knew or should have known" a practice affecting "vulnerable" groups was deceptive, I believe that an intent standard is certainly reasonable in a law that imposes monetary fines on an idividual, and that standard already applies in the FTC Act where penalties are permitted.[10] But the FTC Act is also remedial. It is designed to protect consumers from false advertising and other deceptive practices, not to punish business. On the contrary, the law protects honest competitors from the effects of these practices. The only relevant question in determining whether to challenge a practice should be whether the practice is deceptive, not whether the person engaged in it knows it is.

If a company is engaged in a campaign of false advertising, and this can be proven, it should not also be necessary for the government to show that the company should have known its advertising was false before the false ads can be halted. An advertiser's intent does not mitigate injury to customers and competitors caused by false advertising. Further, the knowlege standard could be read to mean that a businessperson could only know that his or her practices were deceptive if the same practices had been challenged in some other context before. Thus, the change could have the effect of introducing an actual notice requirement into the law, thereby virtually freezing the development of consumer protection at the date of its enactment. It is very possible that the adoption of this standard would make it more, rather than less difficult for the Commission to protect vulnerable groups.

In an effort to respond to many of the concerns I and others have raised about the Chairman's proposals to redefine deception, the Director of the Bureau of Consumer Protection, Timothy J. Muris, has written a lengthy memorandum explaining how the new standards are intended to operate. The primary troubling feature of Mr. Muris' memorandum is not that his explanations concerning how the revised law would operate are not sensible, but is instead that there is no guarantee whatsoever

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whether the word "opinion" is used), then the standard will add nothing to existing law except confusion and litigation as lawyers and judges struggle to determine just what change the new provisions is intended to effect. For an example of existing law that already draws this distinction, see *Koch* v. *FTC,* 206 F. 2d 311 (6th Cir., 1953).

[10] See 15 U.S.C. § 45(m)(1)(B).

that the courts or the Commission could or would apply the standards in the manner he says they are intended to be applied.

For example, the memorandum states: "[A reasonableness] standard, however, would not impose any significant barrier in those cases that the Commission *should* prosecute. It would not require surveys or other extrinsic evidence in all cases, indeed, such evidence would be necessary only in that small class of 'close' cases." (emphasis in original) (page 11)

I find this purported explanation of the way his new statutory standards would be applied facile and hence disturbing. If his standards for case selection were used as internal guidelines by the Commission (which in fact in large measure they are), then I agree with them. That is the way they should work and the Commission tries very diligently to weed out "mistakes" in close cases. But we are here today because it is proposed that these standards be inserted into a statute, and I would only reiterate that if that were done the state and federal courts will not assume that the Congress inserted them for no reason. If a standard as well developed in the case law as "deception" is altered, the courts will rightly assume that Congress intended to change the law. Most of our cases, "good" or "bad," are appealed to the federal courts, which have the last word. It seems distinctly unlikely to me that federal judges, faced with a new statute, will allow the Commission to instruct them about "good" and "bad" and to tell the court when (because the Commission says the case is good) the court should continue to follow previous law and allow inferences of consumer injury and harm, and when (because the case is close) the court should follow the new law and require survey evidence as to an ad's meaning and proof of actual injury and actual harm to consumers. It seems much more likely to me that the new statute would be read to require detailed consumer survey evidence documenting the Commission's interpretation of all allegedly deceptive advertising, however blatant or obviously false the Commission finds it to be. This kind of evidence will be expensive and burdensome to produce—and the advertisers will share that burden with the Commission. The predictable result is fewer cases and far more lengthy proceedings to resolve the few that are brought.

A similar problem arises in Mr. Muris' discussion of how the Commission would go about proving that deception caused "substantial consumer injury." He writes in his memorandum:

"A requirement that the Commission in fact prove that this kind of injury is likely before it finds an ad deceptive is *not* a requirement for quantitative cost-benefit analysis in advertising cases. Nor need injury be measured in monetary terms. Rather, in most instances, a logical inference that injury is likely to exist would suffice, subject, of course, to rebuttal by the respondent's evidence." (emphasis in original) (page 22)

Even assuming that the Commission could distinguish between cases where a "logical inference" of injury would be appropriate and those where it would not and that the courts would accept our distinction without question as within our discretion (which is doubtful), some extensive documentation of injury would almost always be necessary to meet the respondent's inevitable evidence that consumers were not materially harmed by the proven deception. Once again, I emphasize that I agree with Mr. Muris that the Commission should focus its limited resources on cases where deception can cause the greatest injury to consumers. But once we have proven a claim is false, or unsubstantiated, we should not also have to examine what the product was really worth to consumers or what opportunities for benefit they missed by buying it rather than some other product.

In an effort to explain how the proposal would screen out cases where no injury occurred, Mr. Muris cites the recycled oil cases where the Commission found that it was deceptive to sell recycled oil without disclosing that the oil was, in fact, recycled. Since there is no difference in performance between recycled oil and oil refined from virgin crude, Mr. Muris concludes that no injury occurred, despite the Commission's undisputed finding that consumers preferred the produce made from virgin oil. Mr. Muris argues that had consumers realized the equivalence in performance of the two products, they would not have had an irrational preference for the virgin oil. I do not disagree with that conclusion, although Mr. Muris does not explain why sellers of recycled oil could not claim equivalent performance at the time they disclosed that their product was recycled. But I find the implications of his analysis troubling. Is the FTC to become an arbiter of consumer taste, judging what is good or bad for consumers in the guise of an economic analysis of consumer injury? Once again, the courts' inability or unwillingness to follow Mr. Muris' carefully constructed interpretive rules could lead to this result.

I would also point out that Mr. Muris' otherwise thorough memorandum does not discuss the ramifications of his proposal for the Commission's advertising substantiation program. Representatives of two advertising trade associations have informed me that they do not believe the proposal will affect the substantiation doctrine, which is based in large measure on the Commission's deception authority and forms the underpinning of the industry's own self-regulatory program. I believe they are wrong. In order to prove or even to infer injury, as a statutory requirement, the Commission would, it seems to me, have to prove that the claim was false—i.e. that the product lacked the attribute the advertiser or seller claimed for it. It seems quite unlikely that the Commission could show that a claim which was simply unsubstantiated (or made without a reasonable basis to believe it was true—as opposed to being plainly false) caused the kind of concrete, measurable injury that is contemplated by the proposal. Thus, the entire substantiation doctrine would be called into question, if not shortly disregarded.

In closing, I would note that in developing his proposal, the Chairman has identified several past Commission cases which he believes were serious mistakes and which he believes could not be brought under a weakened test for deception. In one of the cases the Chairman cites (Kroger, Docket No. 9012), I dissented from the majority's finding of liability and discussed at some length why I thought the Commission's interpretation of the advertisement as deceptive was misguided. And while that is true and remains my opinion of that case, I do not believe that that dissent, nor any of the other cases cited by the Chairman, supports a modification of the deception standard for several reasons:

First, it makes no sense to me to jeopardize the results of hundreds of good and sensible cases in order to preclude a handful of ill-chosen ones which may have been brought over a 44 year period. Second, the proponents of a weakened deception standard have given absolutely no indication at all of just how their various new standards would operate to eliminate the ill-chosen cases and at the same time enable the pursuit of meritorious cases without making prosecution of such "good" cases excessively burdensome, time-consuming and expensive. For example, if the new standard would operate to prevent one of the allegedly ill-chosen cases by requiring the Commission to produce a survey to prove that consumers relied on a false claim, instead of being able to infer reliance as it now does, then it is fully predictable that courts will similarly read the new standard to require a survey in a strong, meritorious case. While the Commission would theoretically be able to obtain such a survey in a strong case, it has not sought to do so in many cases involving blatantly false claims both because such evidence is not required under current law and because of the substantial time and expense involved.

Undoubtedly the Commission has on occasion brought ill-advised cases, just as other prosecutorial bodies have. But the solution for that problem lies in the exercise of better prosecutorial discretion, not in weakening the law in a way that threatens to make the large majority of justifiable cases much more expensive and difficult to bring. A law long in operation should be changed where there is a potential for serious abuse that can be remedied. In this instance, the proponents of a change in the deception standard have not pointed to any serious abuse, nor do I believe they have thought through the consequences of their proposals on the vast majority of the agency's cases. This is in part, no doubt, because those consequences are, in all honesty, impossible to predict.

I do not believe that most honest businessmen and women have any interest in weakening the laws that prevent deceptive commercial practices. The proposed change, while accomplishing no significant benefit, will enormously complicate, lengthen, and make more expensive the task of FTC attorneys who must endeavor on dwindling resources to prevent deceptive practices. Especially at a time when we have pledged to deliver to the public more value for less money, I must take strong issue with a legislative proposal that will almost certainly effect the opposite result.

Thank you. I will be pleased to answer any questions you may have.

[The following information was subsequently received for the record:]

Federal Trade Commission,
Washington, D.C., August 30, 1982.

Hon. Robert W. Kasten,
Chairman, Committee on Commerce, Science, and Transportation,
Washington, D.C.

Dear Senator Kasten: I am pleased to respond to your letter of August 5, 1982, presenting written questions you wish me to answer for the record of your Committee's July 22 hearings concerning the Federal Trade Commission's authority over deceptive trade practices.

Question 1. Do you agree that the "reasonableness plus injury" test proposed by Chairman Miller should be employed as a case selection criterion? If so, why do you believe it would be so much more difficult if the agency had to convince others that it had selected its cases well? If you disagree with this test for case selection, what kinds of cases that fail to meet the test should the Commission bring? What past cases that fail this test were wise uses of the Commission's resources?

Before responding to these questions, I think I should clarify my understanding of the "reasonableness plus injury" test to which you refer. Chairman Miller has proposed that the Congress limit, by statute, the Commission's legal authority over deceptive trade practices to cases where the Commission can prove that consumers, "acting reasonably in the circumstances", relied "to their detriment" on a "material representation" that "is likely to mislead" them. (emphasis added)[1] He has stated that the phrase "to their detriment" is intended to impose a requirement that the Commission prove that the acts or practices in question are "likely to reduce consumer welfare", or, as I understand it, are likely to injure consumers.[2]

It is my understanding that this proposed statutory language essentially contemplates that the Commission could not find an act or practice deceptive unless it could conclude, on the basis of substantial, empirical evidence, that consumers were acting "reasonably" and were actually injured.

I have said in the past that I agree with some of Chairman Miller's observations about the appropriate standards to be applied in the deception area for case selection purposes. Specifically, I agree that the Commission should not interpret advertising or other sales claims in an unreasonable manner by, for example, reading into the ad implied claims which were never intended to be communicated by the advertiser. Further, as a matter of prosecutorial discretion, I so not believe the Commission should take action where a claim would mislead only the most gullible. Finally, I agree that we should focus our resources on cases involving substantial consumer injury. For an example of my views on these issues, I would refer you to my dissenting statement in the *Kroger* case, D. 9102 (September 25, 1981).

The problems I have with extending these general observations from the arena of case selection criteria to a statutory redefinition of the Commission's deception authority are twofold.

First, out of the context of a specific case, it is extremely difficult to articulate in a single statutory definition what constitutes "reasonable" behavior or "significant consumer injury". Second, the Commission and the courts have been considerig these issues for 44 years and a substantial body of case law has developed giving meaning to these terms. However, Chairman Miller has stated on several occasions that his intention is to oveturn much of this precedent and to substitute a different definition of deception. If the Congress were to adopt his proposals to redefine and narrow the Commission's deception authority, the Commission and the courts would be cast adrift from established precedent to search for the new law's meaning. I do not believe that the Comission's past record, under the guidance of the federal courts of appeal, justifies such drastic action; in fact, a careful study of the development of the law of deception leads me to the opposite conclusion. The Commission and the courts have done a credible, responsible job of establishing appropriate legal standards over the past 44 years which are sufficiently clear to enable businesses to gauge the appropriateness of their conduct, while at the same time retaining enough flexibility to adapt the law to changing commercial circumstances.

Perhaps some examples of how past cases might be analyzed under the Chairman's new definition of deception would help to illustrate my concerns.

The Chairman has stated that the Listerine case, involving false claims that the product would prevent or cure colds, was correctly decided.[3] But he disagrees with the Commission's decision in the Poli-Grip case, which involved false claims that the product would eliminate discomfort and embarrassment when denture wearers ate "problem" foods such as apples.[4] His reasoning for opposing the Poli-Grip case is that the product is inexpensive, is purchased frequently and the claims concerning its efficacy are relatively easy to evaluate. It is apparently his view that this particular precedent would be eliminated by the new statutory definition of deception because the Commission would have difficulty showing that the admittedly false claims for the product caused significant consumer injury.

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[1] Prepared Statement of James C. Miller III, Chairman, Federal Trade Commission, before the Committee on Commerce, Science and Transportation, Consumer Subcommittee, United States Senate, July 22, 1982, at page 4.

[2] Id. at page 6. Chairman Miller has also proposed an additional, alternative test for deception: that is, an act or practice should be defined as deceptive if it constitutes a "material representation" that "the representor knew or should have known would be misleading." He has stated that under this second, alternative "knowledge" test, the Commission would not be required to show a likelihood of consumer injury. Id. at page 4.

[3] Id. at page 22.

[4] Id. at page 37.

Listerine mouthwash is also the type of product which is relatively inexpensive and purchased frequently. What, then, is the distinction between the two cases that would permit one to survive under the new definition of deception while the other would not? Even if consumers were able to judge after the first purchase whether or not the claims made for the product were true, substantiated or false and deceptive—and it is not at all clear to me that they would be able to do that in either of the above cases—the injury caused not only to consumers but also to competitors after even one purchase by deceived consumers could amount, in the aggregate, to millions of dollars of unjust enrichment to a business engaging in deceptive practices. Further, I do not believe we should ignore the significance to consumers and to the advertising industry of the perhaps intangible, but nonetheless important, value of preserving the integrity of commercial advertising against the erosion of credibility that would occur if admittedly false claims could be disseminated without fear of prosecution so long as the item was "relatively inexpensive" and "frequently purchased".

With regard to the second part of your first question ("If so, why do you believe it would be so much more difficult if the agency had to convince others that it had selected cases well?"), it should be clearly understood that the Commission *now* must always be prepared—and most often is called upon to convince a federal court that it selected its cases well and, furthermore, that it proved what it charged, whether it alleged that the claims involved were false, deceptive, unsubstantiated or whatever. Every decision of the Commission finding a respondent's activities to be deceptive can be (and most are) appealed to the federal courts before whom we must justify our actions and display our proof. The courts, not the Commission, are the final arbiters of the meaning of deception and the appropriateness of FTC decisions.

In conclusion, I oppose the Chairman's proposal not because I object to the application of some of the principles he espouses in the context of case selection, but rather because the language he has proposed to codify these principals is susceptible to several alternative meanings and it is by no means clear how the new law would be interpreted by the courts. Any effort to redefine deception would cause great legal uncertainty and would adversely affect not only the Commission and consumers, but also the businesses we regulate. In the final analysis, I would urge the Congress to rely on its own oversight and confirmation processes and the required review of Commission decisions by the federal courts as effective external controls on the Commission's prosecutorial discretion.

Question 2. Is there a difference between "unfair" and "deceptive" advertising? Are these separable legal concepts?

My answer to both questions is yes. Historically, although many of the Commission's complaints have included allegations that the practices at issue were both deceptive and unfair, the Commission's development of the two doctrines has proceeded along clearly separate and distinguishable lines. The cases discussed in the Commission's December 22, 1982, Policy Statement on unfairness, for example, all contained explanations of the standards the Commission uses in determining whether a practice is unfair. In drafting that Policy Statement, we were careful to cite only the aspects of the cases which concerned the Commission's unfairness, as opposed to its deception, authority.

It is, of course, possible for a single act or practice to be both unfair and deceptive. However, the legal standards the Commission would apply in arriving at such conclusions are entirely different. At the risk of oversimplifying, a claim is considered deceptive if it is false, misleading or contains a material omission of fact. A practice is considered unfair if it causes substantial consumer injury which consumers could not reasonably have avoided and which is not outweighed by countervailing benefits to consumers or competition. In determining whether a practice is unfair, the Commission will consider relevant public policies established by state or federal legislative bodies, business organizations or other institutions.

During the Committee's hearings, the point was made that because the reauthorization legislation recently adopted by the full Commerce Committee both codifies the Commission's definition of unfairness and eliminates our jurisdiction over unfair advertising, the committee should not also at the same time redefine and narrow the FTC's deception authority. Until the Congress, the Commission and the courts have had some experience with the impact of these changes in the FTC's unfairness authority, it would be unwise to adopt any of the numerous proposals which have been made to narrow our authority over deceptive trade practices.

I hope my responses to your questions are helpful to the Committee. Please contact me if I can be of any further assistance.

Sincerely,

Patricia P. Bailey, *Commissioner.*

Senator **Cannon**. Thank you, Commissioner Bailey.

Commissioner Pertschuk.

Mr. **Pertschuk**. Thank you, Mr. Chairman. I am delighted to join with the Republican majority of the Commission in espousing an essentially conservative position, that a law which has existed and served consumers well for 44 years, which is not broken, ought not to be fixed without some very substantial burden being met by those who would advocate change.

I am also, frankly, very puzzled. You have a statement that I prepared for the record which I would like to submit.

Senator **Cannon**. It will be made a part of the record in full.

Mr. **Pertschuk**. Thank you, Mr. Chairman.

My statement attempts to respond, and I think fairly, to the statements of Chairman Miller and Tim Muris who is the Bureau Director as to what they are after in changes of the law and why the law needs to be changed and how the law would be changed.

I find this morning, as Commissioner Bailey has pointed out, that the Chairman has shifted substantially in his definition and in a sense we have been moving with a shifting target. I think that in fairness the Chairman has been attempting to respond to the various criticisms and questions raised, but it is very confusing and it is a proposal that is offered in the name of clarification and certainty, and I find the more I get into it, the more confused I get.

There seem to be two problems, two basic problems, the Chairman is concerned about: That the law would theoretically permit the Commission to pursue foolish cases, to interpret ads in a silly and foolish way, and the Chairman and others cite dictum from cases decades ago and they cite a few cases, the majority of them going back to the 1940s which they think are silly and may very well have been silly, but I do not really think that is law.

David quoted from the Commission decision, his statement on the law in 1963, which essentially discards the idea that the Commission can really defend the foolish. If I may, let me just quote a little further from the same decision that David cited, which is our law.

It says:

> Of course it has been reiterated many times that the Commission's responsibility is to prevent deception of the gullible and credulous as well as the cautious and knowledgeable.

That is supposedly the terrible language that has to be fixed.

> The principle loses its validity, however, if it is applied uncritically or pushed to an absurd extreme. An advertiser cannot be charged with liability in respect of every conceivable misconception however outlandish to which his representations might be subject among the foolish or feebleminded. Some people because of ignorance or incomprehension may be misled by even a scrupulously honest claim. Perhaps a few misguided souls believe, for example, that all "Danish pastry is made in Denmark." Is it therefore an actionable deception to advertise Danish pastry when it is made in this country? Of course not. A representation does not become false and deceptive merely because it will be unreasonably misunderstood by an insignifi-

> cant and unrepresentative segment of the class of persons to whom the representation is addressed.
>
> If however advertising is aimed at an especially susceptible group of people such as children, its truthfulness must be measured by the impact it will make on them, not others to whom it is not primarily directed.

That is the law. That is the Commission's decision. That governs our decisions today.

And the Commission has followed those practices. That is the other question. If it is not broken, do not fix it. Calvin Collier will testify later. I have had a sneak preview of his testimony. He is a very fine lawyer. He is elegant in his arguments. He basically says the Commission has already been following the standards that are embodied in Chairman Miller's proposal. It has been following it for at least the last 10 years. Therefore, it is perfectly reasonable to put it into the law.

I accept the first part of that statement, but I do not really go along with the second because there are risks. At various times, Chairman Miller, and Muris and other advocates have basically set up new standards of proof in defining what their intention is, which could impose enormous burdens on the Commission.

Proof of injury: We really do not know what that means, but it could mean that the Commission would have to adopt enormously expensive survey tactics in order to go ahead with cases, and it could mean that the Commission's cases, past and present, would be subject to enormous risk of judicial interpretation of a new standard.

The courts are not going to say that Congress went through this enormous energy of changing a basic law to do nothing, to simply codify the existing law. There must have been a reason why Congress acted. And that opens up an area for mischief.

Mr. Chairman, I see that my time is expiring. The real question is: Why are we here? Up until this year, nobody, to my knowledge, nobody—not scholars, not Commissioners, not consumers, not trade associations, no Member of the House or Senate—no one was proposing the Commission needed a new legal standard to enable it to focus only on significant cases, that deception needed to be interpreted—no one.

Cal Collier may be right, but he never raised the question as Chairman of the Commission, as General Counsel of the Commission, as a member of the Commission, that deception needed redefining.

Finally, Mr. Chairman, I note—and no one could be more sensitive than I am to the fact that there is a substantial backlash in this country against overregulation and certainly Congress has made its feelings known in that regard, and we see from public polls and other indications—that the public feels there is too much regulation.

But the one area consistently that does not meet with public disapproval is the regulation of advertising. Consistently the polls show the public feels that they need more and stronger regulation of deception and unfairness and overreaching in advertising. They want that kind of regulation. This proposal can do nothing but weaken the government's ability to police advertising for deception.

Thank you, Mr. Chairman.

[The statement follows:]

STATEMENT OF HON. MICHAEL PERTSCHUK, COMMISSIONER, FEDERAL TRADE COMMISSION

The Chairman's proposal to amend Section 5 to specify which practices are "deceptive" is as extraordinarily complex as it is novel. In general, I think it is a well intentioned effort to embody a conservative political ideology into the country's principal consumer protection statute, but with very little appreciation of the risks of doing so. Unfortunately, since the Chairman and now the advertising associations have embraced the proposal, we must take it seriously and try to understand how drastically it would change current law.

Before I discuss the Miller proposal, however, it is useful to review the existing legal standard for "deceptive" practices that has evolved over more than forty years of Commission and court cases. A practice is deceptive if it has a "tendency or capacity" to mislead consumers.[1] The misleading practices must concern practices which are "material," that is something which makes a difference to people in their purchasing decisions.[2] "Puffing," that is, statements that are so vague or exaggerated as not to be taken seriously, are excluded. There is no need to prove that the seller intended to mislead anyone.[3] The tendency to deceive is not evaluated on the basis of what an average or "reasonable" person believes but if it would deceive even unsophisticated consumers.[4] It has never been required that the Commission prove actual injury to consumers, only to prove that practices had a tendency to deceive people. Consequently, harm to competitors or to the integrity of advertising generally has been a sufficient basis for prohibiting deception. Finally, the Commission, subject to the review of the courts, has always been able to analyze claims to determine if they are likely to deceive consumers without contracting for elaborate statistical surveys of the consuming public to establish how many people were actually misled. Evidence of this sort on either side of the issue is considered, however, and frequently presented.[5] In addition, an advertisement is not deceptive if it will be misunderstood by only an "insignificant and unrepresentative segment of the class of persons to whom the representation is addressed." [6]

These principles have been farily well understood for many years and have served the Commission and the public well, particularly over the last decade. Heretofore, the primary complaint with the Commission's record was that it pursued "trivial" cases, that is, cases against practices which were no doubt technically deceptive, but which didn't affect many people or dealt with information about products that people didn't care about very much. This was the conclusion of the famous 1969 ABA Report, which culminated in a revitalized and aggressive Commission all through the decade of the 70's.

The Commission over the last decade, led by both Republican and Democratic Chairmen, used the existing legal standard to focus on deception which affected millions of consumers, rather than just a few, and which caused major injury. Until a year ago, no one was proposing that the Commission needed a new legal standard to enable it to focus only on "significant" cases. The recent history of the Commission proves just the opposite.

Directly in the path of this historical trend steps Chairman Miller with his very different ideas about what the FTC should do. The cornerstone of his philosophy is embodied in his proposal to amend the deception standard that has been with us since 1938. Although the Commission has never seen actual legislative language which incorporates the Chairman's proposal, I understand it to involve the following changes. Before the Commission could prevail in a deceptive practice case:

The Commission would have to meet a certain standard of proof of consumer injury.

The Commission would have to prove, not only that less alert, but "reasonable" consumers would be misled by the practice.

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[1] See, e.g., *Charles of the Ritz Distributors Corp.* v. *FTC*, 143 F.2d 676, 679 (2d Cir. 1944). Also, see Kintner, A Primer on the Law of Deceptive Practices (1971) at 33.

[2] See, e.g., *FTC* v. *Mary Carter Paint Co.*, 382 U.S. 46 (1965).

[3] *DDD Corp.* v. *FTC*, 125 F.2d 679 (7th Cir. 1942); *Bockenstette* v. *FTC*, 134 F.2d 369 (10th Cir. 1943).

[4] "[T]he fact that a false statement may be obviously false to those who are trained and experienced does not change its character, nor take away its power to deceive others less experienced." *FTC* v. *Standard Education Society*, 302 U.S. 112 (1937).

[5] *Cinderella Career & Finishing Schools, Inc.*, v. *FTC*, 425 F.2d 583, 588 (D.C. Cir. 1970).

[6] Universe Co., 63 FTC 1282, 1290 (1963).

For groups which are "vulnerable" and are not reasonable in interpreting claims, e.g., the elderly and children, the Commission would have to prove knowledge or negligence on the part of the advertiser.

Misleading opinions would be exempt.

Each of these elements has to be analyzed separately to begin to understand the Miller proposal.[7]

CONSUMER INJURY

Miller has made very clear that he feels it's essential to impose a legal requirement that the Commission establish a certain type of injury before we could stop any practice. Although this idea seems to make some sense, in practice it radically changes the nature of Commission enforcement.

First, we should ask what type of injury the Chairman has in mind. Here Chairman Miller and Mr. Muris enter a murky thicket and it becomes difficult to keep up with them. In his Senate testimony, Miller said not only must consumers be hurt, but they must be hurt a lot: "If the product is inexpensive and is something consumers purchase often and can easily evaluate for themselves, the marketplace will work in preventing deceptive ads." [8] For example, says Chairman Miller, a misleading advertisement for denture cream would not be deceptive because elderly consumers would only lose a small amount before they learned the error of trusting the ads.[9]

On this basis it would seem we could conclude that there is no deception unless the Commission could prove consumers had lost quite a bit—$25 maybe, $50? Hard to say. A column in Advertising Age assumed the products would have to cost over $10.[10] But a recent letter from Mr. Muris to Advertising Age says that the products could be inexpensive after all.[11] Since we know Mr. Muris supports the Commission's Listerine case, we can conclude that to violate the law, deceptively sold products must cost more than denture cream as long as they cost as much as mouthwash and their brand of mouthwash costs more than denture cream.

Unless, of course, the injury is not economic. In his House testimony, Chairman Miller says we should only bring cases "in which consumers have been hurt—by spending money, or using time." [12] That sounds like economic injury, but then he adds, "Of course, this injury doesn't always have to be monetary." The Advertisers propose their own striking twist. The injury must cause "substantial economic injury to consumers" unless the advertiser has knowingly lied or engaged in gross negligence. Thus, the advertisers are at least clear that safety risks and emotional injury are exempt unless we can prove something about intent.

We can also be confident that the Miller-Muris proposal does not include economic injury to competitors. That is, if a manufacturer makes a false claim about a small item, say denture cream, and consumers buy millions of them, we can't consider the injury to competitors. The honest advertisers of denture cream can lose sales but the FTC can't stop the false claims which are hurting them. Too bad for the competition.

Must the commission prove tangible injury to consumers or can we assume injury because people are deceived? Mr. Muris says that the key question is whether "consumers have to give up something of value if the claim is false." [13] On this basis, Chairman Miller and Mr. Muris didn't like cases like those involving deceptive pricing where people aren't really "hurt" even though they are being misled about certain information.[14]

If the Miller-Muris standard were that the Commission had to prove consumers had suffered tangible harm. Though unfortunate, it would shed some light of clarity. But Chairman Miller testified that people who bought ordinary hot dogs thinking they were kosher and bread containing sawdust, thinking it was ordinary bread, would be injured under his standard. This would be true even if there were no physical effects from the differences. What would be the injury there, asked Congressman Scheuer:

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[7] The Advertising Associations proposal appears to be basically the same but it does have a few significant differences. I discuss their proposal below also.

[8] Statement to the Subcommittee on Commerce, Transportation and Tourism of the House Committee on Energy and Commerce, April 1, 1982, p. 14.

[9] Miller, "Why FTC Curbs Needed," Advertising Age, March 22, 1982, p. 83.

[10] Advertising Age, June 28, 1982, p. 26.

[11] Advertising Age, July 12, 1982, p. 64.

[12] House testimony, op. cit., p. 13.

[13] See Muris, memorandum to the Chairman, March 25, 1982, p. 22.

[14] Id., pp. 23–25.

Chairman Miller: "Let me speak to the sawdust and kosher hot dogs. I think under my proposed standard for deception there would be injury. There would be psychological injury . . . it would be evidence on its face that somebody had been damaged, that a person who bought the hot dog thinking it was kosher [had been] damaged."[15]

On the other hand, Mr. Muris says the proposed standard would "easily screen out" Commission cases such as deceptive pricing cases. In these cases, which typically involve claims thast a product has been drastically reduced from its "regular" price, Mr. Muris, at least, says this deception is not impoprtant—not even important enough to cause "psychological" damage. Why a false claim of "kosher" causes psychological damage but a false claim about regular prices does not is mysterious.

Now, applying the Miller standards—which we are urged to adopt because of their clarity—how would the Commission deal with the following:

(a) A false claim that a cigarette did not contain tar or nicotine?

(b) A false claim that a food contained no cholesterol or other fats?

It's hard to say what we would have to prove under the Miller-Muris proposal. It could be that the Commission would have to prove that cigarettes actuallly caused cancer in order to stop the first claim. That burden could be met, because of the overwhelming scientific evidence, though the tobacco industry would be the last to agree. But that's the exception. How about proving tha cholseterol was bad for people? That's a scientific debate that has gone on for years and won't be proved or disproved in a FTC case. But Chairman Miller's standard could mean that a flatly false claim that a food had no cholesterol couldn't be stopped. Maybe, Chairman Miller would say it's not exempt because there's "psychological injury." But why some deception causes psychological injury and some does not is hard to understand.

In summary, the Miller test for injury is like a puzzle that is solved by looking at clues to find out what it does and doesn't cover. It does cover claims about kosher hot dogs because there is "psychological damage" but it doesn't cover all cases where people are misled. It doesn't cover denture cream because it's inexpensive but the product doesn't have to cost $10. It covers false claims about sawdust in bread, but it doesn't cover false claims about "regular prices." It recognizes injury to consumers which is not "economic" but it doesn't cover injury to competitors or to the integrity of the marketplace.

Another very tricky aspect of the Miller proposal is the requirment that the Commission prove consumers relied on the claim.[16] To take our cholesterol claim example, the Chairman is apparently saying that the commission must obtain a survey of some sort to insure that consumers bought, say, "Health Way" bacon because the manufacturer claimed it had no cholesterol. Under the existing standard, Commission lawyers would be expected to show only that "Health Way" bacon, after all, really did contain fats. Everybody in the room would rightly assume the claim was masterial and had a tendency to deceive. Under the Miller standard, Commission lawyers might have to hire a market survey firm first to launch a survey of contented (but misled) "Health Way" bacon eaters to ascertain why they bought it.

Perhaps realizing that the whole idea of proving injury is complicated, Mr. Muris' most recent statement about injury is that the question really amounts to whether consumers "do not get what they want."[17] Happily, he sounds like he's getting at the current deception standard. If the question is simply whether consumers are likely to be misled, we don't need to change the law.

In short, there are a lot of questions about the injury standard, but this debate is only the first element of the new standard offered in the name of introducing clarity into the law. But that's just the beginning of the maze.

REASONABLENESS AND VULNERABLE GROUPS

The second component of the Chairman's proposal is the idea that the Commission should measure deception only by whether reasonable consumers are likely to be deceived. What is the Chairman getting at? One possibility would be that a claim should be interpreted only as a majority of people do. However, Mr. Muris has said "any claim may have more than one reasonable interpretation," so apparently the standard would not require that a majority of consumers would be deceived. Indeed, the number of consumers deceived does not seem to be determinative at all. What matters is that those who are deceived are "reasonable people."

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[15] Testimony before the Subcommittee on Commerce, Transportation and Tourism of the House Committee on Energy and Commerce, April 1, 1982, p. 61.

[16] See Muris memorandum, p. 22.

[17] Advertising Age, July 12, 1982, p. 64.

But how should the Commission determine reasonableness? Must the Commission obtain statistical surveys in order to interpret all ad claims? Mr. Muris has said that the "interpretation of advertising should not be left soley to the subjective judgments of the Commissioners." However, in discussing the practicality of his own proposal, he also says, "In most appropriate cases, the advertisement itself may be the only evidence necessary" to determine how it would be understood by reasonable consumers. In other words, then—as now—the Commission will generally know what an ad means when it sees it.

Mr. Muris doesn't tell us why some claims should obviously be interpreted in a certain way and some should not so it's instructive to consider an example of an ad where he believes the meaning is "apparent on the face of the advertisement itself." He suggests this example: "[O]ur product will kill bacteria. Take it when you feel your next cold coming on." It is likely, he says, that this is a claim that the product will prevent colds. I might interpret the ad this way and so apparently does Muris, but it's not at all clear that the company would agree. In fact, this is the very kind of dispute that lawyers love and companies pay large fees for them to pursue. (I have no doubt some enterprising lawyer will argue the claim can't be read that way because colds are caused by viruses, in addition to assorted other arguments!) What Chairman Miller and Mr. Muris are hoping is that courts will agree with them about what's reasonable. Of course, the courts will on some and won't on others, but precious few will be obvious. For those that are not, it is not at all clear what kind of evidence they would require the Commission to have under the Miller-Muris law.[18]

Chairman Miller does seem to object to the population the Commission has included within its protection in the past. What rankles them is the Commission's occassional willingness to consider how claims might be viewed by "that vast multitude which includes the ignorant, the unthinking and the credulous." [19]

The ignorant, the unthinking, and the credulous do not fit well in an economist's view of the world. They do not behave predictably, and they do not contribute to the efficient functioning of the marketplace. However, who among us (or at least our friends and relatives) had not been ignorant, unthinking, or credulous on occasion, or preoccupied with matters more central to our well-being than the optimum brand of analgesics. It is just such inattention that advertisers often seek to exploit. I suspect Chairman Miller realizes it does not set well with Congress to exclude such persons entirely from the protections the government offers the constantly alert consumer.

Thus, the Miller-Muris proposal includes a special provision to protect "vulnerable groups." The principal savings clause for vulnerable groups is that the Commission can stop an ad if it can show that the advertiser "knew or should have known" that the ad would mislead a vulnerable group of consumers. The Commission should have no trouble satisfying this standard, they assure us, because it is done all the time in tort cases (not to mention criminal cases).

The idea of determining that an ad is addressed to a "vulnerable group" can be pretty tricky, however—both in deciding who's vulnerable and in deciding who's the principal audience.[20]

In addition, intent is notoriously difficult to prove. Consequently, until now, it has been accepted without question by the advertising community and the Commission that the intent of the advertiser is irrelevant to stopping a false claim. Until now, no one has proposed that we should have to establish that a seller of quack arthritis cures knew that his product wouldn't work before the Commission could stop his ads. Most will swear mightily that they sure believe that they work. For Miller, their good intentions are enough.

What I think Miller and the advertisers primarily have in mind is that they don't like the Commission scrutinizing ads for implied claims. They like the approach of requiring the Commission to conduct expensive, national surveys to see how ads were interpreted. And at least Chairman Miller would like to see that happen with a greatly reduced budget. The result will almost certainly be lengthy litigation, endless disputes about the validity of the surveys, and, most importantly, a general slackening in the resolves of advertisers to worry about government scrutiny. Consequently, Miller's elusive search for what "reasonable" consumers think would primarily result in hamstringing the Commission's ability to enforce the law.

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[18] Under current law the Commission is able to conclude an ad's meaning by examining it but will consider evidence if appropriate. Chairman Miller says that in the Ford case the Commission said, "it should ignore a survey Ford produced." Actually, the survey was considered by the trial judge in a summary judgment motion and the judge decided the motion against Ford. The Commission did not reverse that ruling.

[19] *Charles of the Ritz Distributors Corp.* v. *FTC,* 143 F. 2d 676, 679 (2d Cir. 1944).

[20] If the Commission couldn't establish the target group was "vulnerable" and didn't have enough evidence to establish how "reasonable" people viewed the ad, the claim couldn't be stopped even if it was clear the claim was false and the advertiser intended to deceive people!

EXEMPTING OPINIONS

The third component of Miller's deception proposal is that the Commission can't challenge opinions. A Miller press release says that he wants to prosecute "representations of fact" but not "mere statements of opinion." [21] Mr. Muris says we should exempt "claims about which reasonable persons would disagree if they possessed all the facts, provided that the claim itself gives a fairly clear indication that it is merely opinion." [22]

In understanding the proposal, we might begin by asking, what's an "opinion." Chairman Miller testified:

> An opinion is something that is not fact. Essentially you cannot test it. Whether a particular statement is a fact or an opinion is the kind of distinction that would have to be drawn.[23]

That would seem to include the claim, "we believe you'll get 50 miles per gallon in our new Economobile," as well as any other claim where an honest belief was being claimed.

Possibly aware of the implications of all this, Chairman Miller adds a host of qualifications and exceptions to the rather startling idea of exempting opinions. First, to be an exempt opinion, it must be "correctly stated." Second, the person holding the opinion must really believe it. Third, the person must not "misrepresent the degree of his expertise." Finally, the "extent" of the opinion must not be overstated. All these exceptions sound like the Chairman is straining hard to restate current law—by saying opinions are "exempt" if they're not deceptive.

I do believe, however, that Chairman Miller has a real change in mind, but that he's chasing a small gnat with a very large cannon and threatening to shoot a lot of elephants in the process. I agree that some "opinion" claims are really "puffery," or they're so vague there is no tendency to deceive. The law already recognizes these situations. But Chairman Miller wants to exempt opinion claims, if sincerely and accurately stated, even if almost all other evidence pointed toward an opposite conclusion. Imagine a claim by a scientist in an ad that "Red Cross" brand cigarettes are good for you. Mr. Muris says this claim could be challenged because "there is no reasonable disagreement" that cigarettes have adverse health consequences. That may be, though it's a pretty extreme example. But what about a claim that "Red Cross" cigarettes don't cause cancer? Are we really confident that there is no "reasonable" disagreement about this under the Miller standard? How about a scientist's claim that cholesterol in a certain type of potato chip is good for you? The fact is that such claims are misleading without a fuller disclosure of the actual evidence on such important health and nutritional issues.

Maybe Chairman Miller believes that such an opinion claim is "exempt" so long as the full story is given, but that's another way of stating current law. If that's his view, I agree, but we don't have to change the statute.

CONCLUSION

After struggling with the Miller proposal, I have come to the tentative conclusion that the Chairman and Mr. Muris are engaged in a wistful exercise of seeking outcomes they like in particular cases by imposing radical changes in the legal standard for judging all cases. Their proposal does serve as something of a learning exercise for us all and, if it's left at that, we may actually have benefited. But the attempt to economically fine-tune the FTC statute, in a futile effort to achieve "efficiency" in law enforcement, could hobble the FTC, and degrade advertising in our country.

[The following information was subsequently received for the record:]

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[21] FTC press release, March 18, 1982.

[22] Muris memorandum, p. 18.

[23] Hearings Before the Committee on Commerce Science and Transportation, U.S. Senate, March 18, 1982, p. 13.

Federal Trade Commission,
Washington, D.C., September 3, 1982.

Hon. **Robert W. Kasten**, Jr.,
Chairman, Committee on Commerce, Science, and Transportation,
Washington, D.C.

Dear Mr. Chairman: This letter is in response to the two questions you sent to me on August 5, 1982, following up on your committee's hearing on deception on July 22.

Question 1. Do you agree that the "reasonableness plus injury" test proposed by Chairman Miller should be employed as a case selection criterion? If so, why do you believe it would be so much more difficult if the agency had to convince others that it had selected its cases well? If you disagree with this test for case selection, what kinds of cases that fail to meet the test should the Commission bring? What past cases that fail this test were wise uses of the Commission's resources?

1. I am in agreement with the notion that, as a matter of prosecutorial discretion, the Commission should generally bring cases only when it finds evidence that consumers or competition has been injured by a company's deceptive practices. But for several reasons, I take issue with the Chairman's "reasonableness plus injury" test as a statutory standard for "deception" under Section 5 of the FTC Act.

First of all, I should note that even the Chairman recognizes that blatant misrepresentation should be sufficient alone—without a showing of injury—to establish deception. He provides for this with the second prong of his definition: "the representor knew or should have known [that a material representation] would be misleading."

Putting that issue aside, then, the strongest disagreement I have with a "resonableness plus injury" test is with the first half of that standard. The "reasonableness" requirement would withdraw from FTC protection that large minority (perhaps, indeed, majority) of consumers who are not always completely attentive and rational in making purchase decisions. The Chairman believes his standard is necessary to prevent the Commission from pursuing ads that will deceive only the most gone much too far to solve a problem that does not really exist. While the courts many years ago were extremely deferential to the Commission in its interpretation of ads and in its adoption of assumption about how consumers behave, the age of unquestioning judicial deference has passed, as the Chairman himself has pointed out recently. Moreover, the Commission itself has recognized that an ad is not deceptive if it will be misunderstood by only an "insignificant and unrepresentative segment of the class of persons to whom the representation is addressed." Universe Co., 63 FTC 1282, 1290 (1963). Therefore, I feel that a "reasonable" requirement would make no positive contribution to the legal standard, but woud create a whole new area of mischief for defense lawyers, and reduce the protection available to normal consumers who are not always entirely reasonable.

As to an injury requirement, there is still total confusion over the degree and nature of injury that would have to be proven under the Chairman's standard. He has said that he would prosecute deceptive claims for some low-ticket items (e.g., hot dogs and mouthwash) but not others (denture adhesives). The statutory language he proposed at the July 22 hearing refers simply to consumers being mislead "to their detriment." While a major impetus for the Chairman's proposal has been his perception that the Commission has sought to remedy trivial harms, this language would not seem to address this concern at all. Perhaps the explanation can be found in his July 22 testimony at pp. 35-36, where he concludes that as to items that consumers can evaluate themselves at low cost, "the market works—deception is not a viable business strategy." How comforting it must be to believe that the market will eliminate all such deception! But in fact, the market is crowded with deceptive claims for low-cost items; and it is foolhardy to shield them totally from Commission authority.

This issue brings me to a related, and very important, point. The injury to consumers from some deceptive practices may admittedly be relatively small or short-lived. However, such practices can be very damaging to honest competitors and to the business community as a whole, because it diverts customers from legitimate businesses and undermines the consumer's belief in a marketplace that adheres to certain principles of honesty and fair-dealing. I take strong exception to the Chairman's assertion that the Commission should not have an independent interest in these effects. Indeed, I think the business community looks to the Commission to maintain a certain modicum of civilization in the marketplace and strongly supports its efforts in this regard.

I have one additional concern relating to the injury requirement. The Chairman's proposal that consumers must be mislead to their detriment suggests that, as an element of the injury test, the Commission must prove reliance on a deceptive claim. If this is so, it creates a tremendous burden, indeed an insurmountable burden, for the Commission. So many different factors go into a consumer's choice among competing products that no one factor can be isolated as being responsible for a purchase decision.

These are my objections to codification of a "reasonableness plus (consumer) injury" standard. I hasten to note that this phrase does not encompass all of the Chairman's proposal. He has also proposed replacing the "tendency or capacity to deceive" standard with a requirement that the Commission prove that a claim is likely to mislead consumers. This would increase the Commission's evidentiary burden substantially and, combined with the requirement that the Commission prove that those consumers likely to be deceived are reasonable people, would increase enormously the Commission resources that would have to be devoted to litigating a typical case.

You have asked what past cases that would have failed Chairman Miller's test were wise uses of the Commission's resources. Of course, since his proposal raises the proof requirements for successful litigation in several ways, I have to assume that a great many of our cases as tried under the current standard would have failed to satisfy his standard. But in many of them, presumably the standard could have been met by the introduction of additional evidence, albeit expensively acquired evidence. I will not attempt to identify those cases and, because I find the Chairman's proposal far from crystal clear, I will limit my answer to a few cases that necessarily would fail under the new standard, according to the Chairman himself (or his Bureau Director, Tim Muris).

Vega case. The Chairman has said that correctly stated expert opinion claims should not be challenged. His example of an ill-advised case is the "Vega" settlement with General Motors in 1975 (85 FTC 27), in which the Commission's order prohibited G.M. from claiming that any car is superior in handling unless the company has test results to support the claim. According to the Chairman, this case never should have come up—and presumably he thinks it would fail to meet his standard—because subjective claims (in this case, "handling") seldom, if ever, cause injury, and neither do the correctly stated opinions of experts. I disagree on both points.

Polident case. The Chairman has said that when consumers can evaluate products at low cost, there is no injury from false claims about them. He has said that his proposal would prevent cases like Block Drug, 90 FTC 893 (1977), in which the Commissioner challenged claims about a denture adhesive.

I think that bringing an occasional challenge to a highly exaggerated claim about an important product characteristic of an inexpensive product is a good enforcement strategy. No advertiser should feel immune from prosecution simply because its product is relatively inexpensive. I don't think Congress would be doing a service to consumers or to honest businesses by creating a legal exemption for false claims for inexpensive products.

Moreover, there was injury from Block's advertising. The Commission found in that case that substantial trade had been diverted from Block's competitors. Also, in addition to spending money on a product they might not otherwise have bought, many thousands of consumers—a large proportion of which were elderly—may have suffered discomfort and embarrassment from relying on claims made for Polident.

Ford Motor Co. The Chairman has attacked Commissioner Dole's opinion for a unanimous Commission in Ford Motor Co., 87 FTC 756 (1976), as adopting a strained interpretation of advertising—one that a reasonable consumer would not make. One ad at issue in that case discussed gas consumption of Ford cars in a highway mileage test. The ad explained that the cars tested "were regular production models with standard engines and transmissions. They weren't brand new. They were broken in to simulate 6,000 miles of driving. All the cars used regular gas and had normal preparations. The drivers were not professionals and they did not exceed 50 MPH * * *." It also noted: "Of course, the mileage you get may be less or even more depending on many factors: equipment, engine displacement, total vehicle weight, road conditions and your driving style." Because of the second statement, the Chairman has challenged the Commission's conclusion that "this group of statements has the capacity to lead consumers to believe that the test conditions and the mileage obtained by respondent's automobiles in the test represent the type of performance a consumer might expect in normal driving during a long or cross-country trip." 87 FTC at 796.

This case well illustrates some of the problems that the Chairman's proposal would create. To me, the Commission adopted a reasonable interpretation of the ad; to him, the interpretation was strained. The Administrative Law Judge in his initial decision discussed a copy test that in his opinion supported the interpretation adopted by the Commission: "Notwithstanding the analysis of the surveyors, the verbatim responses of the interviewees clearly demonstrate that a great number of them equated the mileage claims with what they ('YOU') might expect to obtain." 87 FTC at 779. (emphasis added) The Chairman, in his July 22 testimony, said that the survey "suggested reasonable consumers did not so interpret the ads." (p. 14) Apparently, he would not find deception when an ad "may mislead some, but not the overwhelming majority." (p. 10) (emphasis added) I feel that an ad can be "deceptive" even if far less than a majority of consumers are deceived; in fact, I don't think you can really determine whether an interpretation is reasonable by finding out how many people adopt it. An ad can have several reasonable interpretations.

Kroger. I continue to support the Commission's decision in Kroger, D. 9102 (Sept. 25, 1981, appeal pending). This case dealt with a major supermarket chain's failure to substantiate its claims that its prices were lower overall for food. Because the claims dealt with weekly grocery purchases, the case addressed economic injury to many thousands of families because of their reliance on unsupported price claims. The evidence showed that Kroger's own internal surveys, actually much more reliable than the advertised survey, demonstrated that Kroger was often not the low price competitor when it claimed to be. The order in that case required Kroger to choose items in a more representative way when it advertised survey-based price claims in the future—a sensible requirement and one that Kroger can follow, probably by relying on a survey it was already doing.

Question 2. Is there a difference between "unfair" and "deceptive" advertising? Are these separable legal concepts?

2. In response to your second set of questions, "unfair" and "deceptive" are quite separable legal concepts, and both should be maintained as separate legal standards under Section 5. While it may be argued that most, or even all, unfair advertising can also be shown to be deceptive, this approach results often in a strained theory of deception that may not be accepted by the courts.

The prohibition on unfair practices in Section 5 is a recognition that consumer injury can flow from actions that are not overly deceptive. Liquor advertising directed to children, for example, might not be any more deceptive than that directed to adults. Nevertheless, such advertising would be unfair because children should not be encouraged to drink even though adults are allowed the freedom to do so.

The Commission's advertising substantiation doctrine provides another illustration of the distinction between unfairness and deception. In some cases the Commission has found an implied representation in advertising that the advertiser had a "reasonable basis" for its product performance claims. In such cases, the Commission has rested its decision, at least in the alternative, on a deception theory. However, in the first ad substantiation case (Pfizer, Inc., 81 FTC 23 (1972)) the Commission expressly disavowed a finding that the advertising was deceptive. Instead, it declared:

> The consumer is entitled, as a matter of *marketplace fairness,* to rely upon the manufacturer to have a "reasonable basis" for making performance claims. A consumer should not be compelled to enter into an economic gamble to determine whether a product will or will not perform as represented. The economic gamble involved in a consumer's reliance upon affirmative product claims is created by the vendors' activities, and cannot be easily avoided by consumers. Taking a different and analytical perspective and weighing the minimal cost and burden on vendors by requiring that there be a reasonable basis for affirmative product claims, against economic losses to consumers which can fairly be ascribed to advertising claims lacking such reasonable basis (losses which are, in a practical sense, unavoidable for the consumer), it is likewise clear that *economic fairness* requires that this obligation be imposed on vendors. (emphasis added)

The unfairness basis for the Commission's ad substantiation requirement is not merely an elegant theoretical construct, interesting only for the political theory it espouses. It serves a very practical purposes: using it allows the Commission to require advertisers to have a reasonable basis for product claims without the Commission having to go through an elaborate showing of proof in each enforcement action that the ad was deceptive. This simplifies enforcement of a legal doctrine that enjoys virtually total consumer and industry support.

An unfairness analysis can also be important in cases where an ad fails to reveal important information about a product, such as an unusual likelihood of harm from a reasonably anticipated use of the product. It can be argued that such an ad is deceptive, on the theory that there is an implied representation of safety in normal use. However, an allegation that the ad is unfair is both easier to prove from a practical standpoint and more straightforward intellectually. It focuses attention where it more properly belongs—on the degree of consumer injury and the countervailing arguments against mandated disclosure.

Thank you for your interest in my views. I hope they will be of assistance to the Committee.

Sincerely,

MICHAEL PERTSCHUK, *Commissioner*

Senator CANNON. What do you think started all this?

Mr. PERTSCHUK. I think somebody had what he thought was a good idea. We have a lot of economists at the Commission these days, Mr. Chairman.

It would be unfair to quote someone as describing economics as a form of brain damage. I would never do that.

In fairness to the chairman, of course he is here to speak for himself, I think there is a genuine concern that the Commission use sensible and economically sound criteria in picking its cases, that it not waste time, that it bring good cases. We do agree with that. David is right.

Much of what the chairman—in fact, most of what the chairman says in terms of what cases ought to be brought I agree with. I think it makes sense and we have been following it and maybe a statement or protocol redefining or setting forth guidelines might be useful, although whenever you start to redefine something which has a history there is always the tendency of creating more confusion than less.

Senator CANNON. Any comments from the other Commissioners on that question?

Ms. BAILEY. Well, I would like to add one thing about what Mike just recently said about Cal Collier's testimony, saying that it ought to be codified because it is what the Commission is doing anyway, that is, to codify the chairman's proposal would not change the law. It would make the law read as the law is.

But to illustrate the confusion around this whole subject, I would say that last week the chairman made a speech in which he said the purpose of the proposal was to change the law. So it is very confusing even for those who have dealt with this law for a long time.

Mr. CLANTON. Very briefly, I believe there is a perception by the chairman and others that there were instances of cases that have been wrongly decided. I think there have been some cases in the past wrongly decided. Certainly I would not purport to sit here and say that everything the Commission has done has been rational, proper and perfect over the last 10 years or 40 years.

The question is: How bad has it been? How far removed from the original congressional intention is it? I do not really see that substantial a departure. I see a fairly consistent body of law over time, although there are cases that the four of us sitting here today could disagree on. An example is the *Kroger* case that the chairman cites, which the Commission issued last year. There were differences there among the four of us as to the ultimate result of that case. I happen to have written the opinion in that case, so I obviously disagree with the chairman's interpretation of the result. Commissioner Bailey on the other hand dissented and would take a position similar to the chairman's interpretation.

That goes to show I think, though, that reasonable people can differ on the question of interpreting a particular advertising claim and deciding a case, but that doesn't necessarily mean the law needs to be changed.

Senator CANNON. Does the Commission have a role in protecting consumers other than reasonable ones?

Mr. CLANTON. I think it certainly does, but I guess I would partly define the question of reasonable as including people who may be in a position not to fully understand the consequences of their actions. It may be ignorance in some instances. I don't view reasonableness as attempting to define what the most rational consumer should be. That is not what the courts have said reasonable standard is.

I think it should be broad enough to take into account classes of consumers who may not have access to adequate information, who may be in a position, as the chairman pointed out in his testimony, of particular vulnerability. I think the *Travel King* case he cited in his testimony was an example of that.

But I think that is a very key point and one I mentioned in my statement that needs to be very clearly understood—that reasonableness is not a term that should be applied only to a select group of people who fully understand the market consequences of a given situation. I think if it is understood in that way, then I think it is broad enough to deal with most of the situations that we would want to deal with.

Senator CANNON. Mike, getting back to your Danish pastry issue, does there have to be a danger of injury before the Commission gets into these cases?

Mr. PERTSCHUK. Generally speaking, the existing law would require as the Commission applies it that the claim be material. That is, that it be a claim which is part of the reason why consumers are likely to buy that product. And the Commission has to infer that the consumers acted or were likely to act on the basis of being misled in making a purchase to their detriment.

These standards are basically the standards applied by the Commission, but the Commission can infer injury. I mean basically taking a look at the reality of the transaction. If in Chairman Miller's case that he cited there is a claim that a product will cure colds and it does not, it is reasonable for the Commission to infer that consumers will believe it and will buy it on that basis.

The concern is with injury; that by adopting an injury test in the statute, the Commission will then have to go out and prove, for example, that consumers who saw a particular ad, for that reason alone, went out and bought the product. That is a terribly difficult mechanical burden to prove. You have to go survey thousands of consumers. There may be lots of reasons. The consumer may not know why he bought the product.

We are talking about advertising. I know an advertiser who says the last thing in the world he wants the consumer to do is to think about the ad. He wants the ad to make an impression and for that impression to basically operate as the consumer goes through the supermarket. That is not necessarily deception, but it does mean the consumer is not always taking a claim, rationally saying I believe this claim, it is important to me, I will go out and buy the product for that reason, and if I lose five bucks, it is because that ad misled me.

Purchasing decisions are more difficult and complex, and to prove a particular causal connection between an ad, a misleading claim in the ad and the actual purchasing decision may make it very difficult, if not impossible, to bring what are on their face deceptive cases.

Senator CANNON. It seems to me that when you were here with the committee a number of years ago, I heard the old argument raised about "if it ain't broke, don't fix it" on many occasions, and that did not seem to have too much effect on you then, but yet I hear you espousing that today.

Mr. PERTSCHUK. I have grown older and wiser, Mr. Chairman.

Senator CANNON. Thank you very much.

Next we will hear from Hon. John J. Easton, Jr., Attorney General of Vermont, for the National Association of Attorneys General.

STATEMENT OF JOHN J. EASTON, JR., ATTORNEY GENERAL OF VERMONT, REPRESENTING THE NATIONAL ASSOCIATION OF ATTORNEYS GENERAL

Mr. EASTON. Good morning, Mr. Chairman.

Senator CANNON. Good morning.

Mr. EASTON. I brought with me a catalog. This was a catalog that we had to deal with in the State of Vermont. The catalog actually advertised a Formula No. 11 providing ingredients that have traditionally been used to strengthen the brain. It lists a number of herbs and they give the dosage. If you have an acute problem, you take 1 tablet every 4 hours, if it is chronic, you take 2 tablets every 4 hours, and if it is chronic to terminal, you take 16 tablets a day.

Senator CANNON. How did you determine whether that was deceptive advertising or not?

Mr. EASTON. We did not have much problem, Mr. Chairman. However, we are concerned, and I am concerned as an attorney general and as one who formerly ran the consumer protection office in Vermont, I am concerned that under these new standards we might have added obstacles and burdens to overcome in order to litigate against this type of catalog. That is why I am here this morning and that is why my colleagues in the National Association of Attorneys General have unanimously supported a resolution opposing changes to the deceptive standard.

Let me just set the stage and tell you what we out in the field, what we lawyers who actually have to enforce these laws do. We bring cases such as the deception contained in this catalog. We bring credit cases for debt collection and repossession, we bring cases for failure to honor warranties, deceptive sales such as mail order and buying clubs. We have pursued deceptive pricing, bait and switch, and going out of business sales.

We at the State level are the lawyers who have to go into court and try cases. Because of this, we are very concerned about the effect that the change in section 5 of the Federal Trade Commission Act might have on our State statutes.

All States have now adopted statutes that prohibit deceptive practices. We are concerned that as a practical matter, as a very practical matter, the State courts will be guided by the volumes of

Federal precedent which occur. There have been some arguments made by Commission staff and perhaps by the chairman that legally the State statutes will not be overruled, that under principles of statutory construction, we will not have a problem in the States.

Well, as I say, first we were concerned about the practical effect. Even if the new amendments to section 5 do not overrule, still on a practical basis, no State is going to be able to enforce standards on national advertising. The State of Texas tried in the General Motors rebate case to pursue a case that the FTC chose not to pursue and was simply not able to do it. So effectively speaking, no State will be able to impose standards other than the national advertising standards determined by the FTC.

Furthermore, the problem is that it is highly unlikely in a legal sense that any State would be able to impose higher standards on local businesses, intrastate businesses, than are imposed on interstate businesses.

We are concerned, as I have said, that these proposals would lower the advertising practices in this country. There would be a reduced standard, it seems to me, of national advertising, and we are concerned about that.

For example, Vermont has a ban against deceptive pricing. Mr. Muris has suggested in his memo, which was filed before this committee in March, that generally deceptive pricing does not cause harm. We are concerned that, if these standards are adopted, then Vermont will not be able to enforce its ban against deceptive practices. We are afraid that there would be a great burden of proof and cost of proof on the States. The costs will be borne not only by the States that have to enforce these laws but also on the businesses that might be affected by these laws.

These additional costs would occur in all cases, not just these marginal cases that the chairman is concerned about, but all cases.

We are also concerned that we would have to relitigate areas of law that have already been litigated in the last 44 years, and are presently clear. I think you have heard from both Commissioner Bailey and Commissioner Pertschuk about the problems of proof. Let me just say that, as the lawyer that would have to go in with surveys, that, surveys are not enough. They are inadmissible hearsay.

Instead, we would have to come in with experts. I think this city is seeing what happened in a criminal case recently when a battle of experts discuss insanity, for example. Well, do we want to impose the same sort of battle of experts over what a reasonable consumer might have perceived or not perceived? And I am afraid that is the burden of proof that would be imposed by this new proposal.

Furthermore, we do not want to have to argue in court whether the consumer behavior was reasonable. Was it reasonable for a consumer to rely on this catalog? Nine thousand consumers around this country did. They sent in their money. Fortunately, we were able to act very quickly and try to recover their money.

I see I am out of time and I will be happy to answer your questions.

Senator CANNON. How much did they sell that product for?

Mr. EASTON. I think they were all generally in the range of $10 to $15. Let's take a look here. I guess the pricing structure is in a different catalog.

Senator CANNON. Was that catalog put out by one organization covering a whole host of products?

Mr. EASTON. It was. It was put out by a business that operated previously in Florida and had moved to Vermont. They did no business in Vermont, so we only became aware as we started getting letters from consumers. One of the letters we did receive, I think, is very helpful. It says:

> Their catalog is full of scripture, yet they took my money knowing they were in financial trouble, I'm sure. My money means much to me. I do not like to be taken by people posing as Christians or others. I do not know whether you can help me with this, but I would appreciate your help.

We were able by moving very swiftly to recover $180,000 that this company had in its account from 9,000 consumers across the country.

Senator CANNON. Senator Gorton, as you heard, was called away to another meeting and asked that I ask some questions here for him. Could not the State attorneys general and the State courts simply refuse to follow any Federal changes?

Mr. EASTON. As I have said, certainly that argument has been raised. However, we are concerned about the practical effect and the lowest common denominator effect, that it is very difficult to impose on national advertising standards different from that imposed on the local level. We think just as a pragmatic effect, 55 percent of the advertising money spent in this country is national, and we at the State level would not be able to impose a different standard.

Senator CANNON. There is a vote in process. I will have to leave to vote, so the hearings will be recessed temporarily until I return or one of the other members.

[Recess.]

Senator KASTEN [presiding]. The committee will come to order.

On behalf of Senator Gorton, Mr. Easton, we would like to continue with this one group of questions.

Is not "deception" a rather vague term? Do we not need legislative clarification to avoid confusion and prevent the FTC from bringing bad cases?

Mr. EASTON. I do not think it is that vague, Senator. Since the statute was enacted some 44 years ago we have got a number of cases interpreting deception. After all, the law consists of both statutes and case law.

The concern would be that if we enacted a new standard it would put deception right back into the same sort of doubt that occurred right after the amendments were passed in 1938. So it seems to me it is pretty clear as to what constitutes deception on the basis of the numerous court interpretations that have been given to the act over the last 44 years.

Senator KASTEN. Are these proposed statutory definitions of "deception" in the best interest of business, in your opinion? What about small business in particular?

Mr. EASTON. That is a good question, Senator, because one of the concerns I have—and I mentioned it during my oral remarks—is the effect of eliminating deceptive pricing from the thought of deception. There has been some suggestion that deceptive pricing cases do not need to be brought under the new definitions of deception, and every deceptive advertising case does have an impact on small business which has to compete with the business using deceptive pricing.

We have a furniture store right now in Vermont that complained to us that one of its competitors is engaged in a going out of business sale. If the allegations are true, the competitor has done 1 year's worth of volume by this phony going out of business sale, in 90 days. We are investigating them and are about to bring a lawsuit. So that is the sort of impact a deceptive advertising case can have on a small business.

Senator Kasten. Mr. Easton, thank you for your testimony. There may be additional questions coming to you from other members of the panel as a result of today's hearing, and we will submit those to you in writing and hope you can get back to us within a reasonable amount of time.

Mr. Easton. I would be happy to do that, Mr. Chairman.

[The statement follows:]

STATEMENT OF JOHN J. EASTON, JR., ATTONEY GENERAL, STATE OF VERMONT

I. INTRODUCTION: A UNIQUE FEDERAL-STATE PARTNERSHIP

Mr. Chairman and the members of the Committee, it is an honor to be here today, to represent the National Association of Attorneys General, who have asked me to present their views of the proposals to amend Section 5(a) of the Federal Trade Commission ("FTC") Act, to define the meaning of "deceptive." On July 18, 1982, the National Association of Attorneys General unanimously passed a resolution opposing changes to the definition of "deceptive acts and practices." The resolution further urged Congress to consult extensively with the states' governors, legislative bodies and attorneys general. (Attached as Appendix A.)

It is encouraging that you seek the counsel of the states' attorneys general in this matter. The prohibition of deceptive acts and practices in the marketplace represents one of the best examples of cooperation between the fedral government and state governments, an implementation of federalism at its best. Since the states are very much partners in this effort, any action by the federal government will affect the states' efforts.

A. The theory of the ban on deceptive parctices.—The premise of the regulation of deceptive acts in the marketplace is that our free enterprise system has as its a basis the informed consumer, able to make an informed choice among a variety of competing products in the marketplace.

The Supreme Court articulated this policy in finding a basis for it in the First Amendment, in *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 765 (1976):

"So long as we preserve a predominantly free enterprise economy, the allocation of our resources will be made through numerous private decisions. It is a matter of public interest that those decisions, in the aggregate, be intelligent and well informed." [1]

The Court also recognized the appropriateness of regulation to prevent the information from being deceptive. Id. at 771-772, n. 24. In fact, the Supreme Court noted as long ago as 1924, "Deception may result from the use of statements not technically false or which may be literally true . . . . It is not difficult to choose statements, designs and devices which will not deceive." *United States.* v. *95 Barrels of Vinegar,*

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[1] The FTC itself has articulated this policy: "It is a basic tenet of our economic system that information in the hands of consumers facilitates rational purchase decisions; and, moreover, is an absolute necessity for efficient functioning of the economy."

Statement of Purpose, Labeling and Advertising of Home Insulation 44, Fed. Reg 50218, 50222 (1979).

265 U.S. 438, 443 (1924). Today, as in 1924, business can appropriately be held to this standard.

Economic theory does not attempt to justify false or misleading information. Such information confuses the market, creates false market incentives by benefitting businesses that deceive consumers, and leads to competition among deveptive claims that are irrelevant to quality or price.

The prohibition of deceptive practices in the marketplace represents a notable consensus among state governments and the federal government. All fifty states and the District of Columbia have enacted statutes to prohibit deceptive representations in consumer transactions. (Appendix B.)[2] These statutes have the FTC Act at their historical and precedential roots. Together with the Section 5 (a)(1) of the Federal Trade Commission ("FTC") Act, this national consensus constitutes an almost unique example of state and federal government working together toward a common goal: honesty in the marketplace. The cooperation is working.

While the federal FTC Act authorizes enforcement only by the FTC itself, the FTC has effectively addressed national and interstate deceptive practices.[3] The FTC Act sets the national ethic for advertising and trade practices.[4] Since there is no private right of action under the FTC Act, the FTC represents only half of the formula.

B. The States' efforts on the Federal model.—The other half of the effort is represented by the remarkable unanimity of state statutes of all fifty states and the District of Columbia. The state statutes are in general modeled after the federal act, which first prohibited deceptive practices in 1938 when the Wheeler Lea amendment was added to the act. Most state uniform legislation is modeled on the Unfair Trade Practices and Consumer Protection law, developed by the FTC in conjunction with the Committee on Suggested State Legislation of the Council of State Governments in 1970.[5] These acts are often called "mini-FTC Acts." In addition, three states have adopted the Uniform Consumer Sales Practices Act, drafted by the American Bar Association.[6] Seven states have enacted the Consumer Fraud Acts.[7] Every state statute prohibits deceptive practices.[8]

All state acts provide for enforcement by state officials; unlike the FTC administrative proceedings, state enforcement is through the state judicial system. State attorneys general are granted authority to enforce the statutory standards through injunctive relief and monetary damages on behalf of their citizens. All but four states[9] provide a private remedy as well. Relief is by civil action, or is available as a defense to a civil action by an offending business, since debtors frequently stop payment because of a deceptive practice in the transaction. Prevailing consumers in these states are usually entitled to attorneys fees. In addition to these judicial enforcement remedies, thirty-five state statutes grant a state agency the authority to issue regulations interpreting the act;[10] sixteen of these states have enacted such regulations implementing important specific principles of the ban on unfair or deceptive.[11]

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[2] National Consumer Law Center, Unfair and Deceptive Acts and Practices (1982), p. 3. In addition, Alabama recently enacted a consumer protection statute.

[3] While insufficient scholarly research has been done, the initial conclusion tends to substantiate this claim. See, Peltzman, The Effects of FTC Advertising Regulation, 24 Journal of Law and Economics 403 (Dec. 1981).

[4] In 1980, advertisers spent $54 billion on advertisements. Of this amount, $30 billion was spent on national advertising, and $24 billion on local advertising. Source: U.S. Dept. of Commerce, Statistical Abstract of the United States—1981, p. 572.

[5] National Consumer Law Center, Unfair and Deceptive Acts and Practices, p. 4–5.

[6] Ohio Rev. Code Ann. § 1345.01 (Baldwin) (amended to prevent unfair practices as well); Utah Code Ann. § 13–11–1; Kan. Stat. Ann. § 50–624 (somewhat modified).

[7] Del. Code Ann., tit. 6, § 2531; Ga. Code Ann. § 106–701; Hawaii Rev. Stat. § 481A; Ill. Rev. Stat. ch. 121½, § 311 (Uniform Deceptive Trade Practices Act § 1); Me. Rev. Stat. Ann. tit. 10, § 1211; Ohio Rev. Code Ann. § 4165 (Baldwin); Okla. Stat. Ann. tit. 78, § 51 (West).

[8] A few state statutes enumerate specific deceptive practices. D.C. Code ch. 28 App. II § 1; Ind. Code Ann. § 24–5–05; Okla. Stat. Ann. tit. 15, § 75.

[9] Arkansas, Iowa, Nevada, North Dakota.

[10] Alaska Stat. § 45.50.491. Ariz. Rev. Stat. Ann. § 44–1526; Ark. Stat. Ann. § 70--902(e); Colo. Rev. Stat. § 6–1–108; Conn. Gen. Stat. §42–110(b); D.C. Code Encycl. ch. 28 App. II § 6 (West); Fla. Stat. Ann. § 501.205 (West); Ga. Code Ann. § 206–1204: Hawaii Rev. Stat. §487–5; Idaho Code §48–604; Ill. Rev. Stat. ch. 121½, § 264 (Consumer Fraud and Deceptive Practices Act § 4); Iowa Code § 714–16.4a; Kan. Stat. Ann. § 50–630; Ky. Rev. Stat. § 367.150; La. Rev. Stat. Ann. § 1405(B) (West); Me. Rev. Stat. Ann. tit. 5, § 208; Md. Com. Law Code Ann. § 13–204; Mass. Gen. Laws Ann. ch. 93A, § 2(C) (West); Mich. Comp. Laws § 445.903(a); Minn. Stat. Ann. §325.80 (West); Mont. Rev. Codes Ann. § 85–403; N.H. Rev. Stat. Ann. § 358–A:4(2); N.J. Stat. Ann. § 56:8–4 (West): N.M. Stat. Ann. § 49–15–11; N.D. Cent. Code § 51–15–05; Ohio Rev. Code Ann. § 1345.05 (Baldwin); Or. Rev. Stat. § 646.608; Pa. Stat. Ann. tit. 73, § 201–3.1 (Purdon); R.I. Gen. Laws § 6–13.1–7(c); S.C. Code § 66–71.7; S.D. Comp. Laws § 37–24–14; Utah Code Ann. §13–11–15; Vt. Stat. Ann. tit. 9, § 2453; W.Va. Code § 46A–6–103; Wis. Stat. § 100.20.

The states have not only unanimoulsy adopted consumer protection acts modeled after the FTC act, they have generally used the FTC model in not providing a strict definition of deceptive. Such a definition would simply provide an opportunity for unscrupulous businesses to avoid application of the act. State statutes generally provide for liberal construction to effectuate the purposes of the acts. State courts, which are the adjudicative bodies for state statutes, have used the act as an effective approach to prevent abuses.

The FTC act provides an inextricable part of this cooperative federalism. First, FTC precedent provides a thorough body of precedent as to what constitutes an unfair or deceptive trade practice. It is "the most significant source of interpretations of deception and unfairness" for the state courts.[12] Nineteen states specifically provide for FTC and federal rulings as a source of precedent.[13] In addition, state courts, with and without this statutory provision, have used the FTC and federal court decisions under the Act as precedent.[14]

Second, the FTC provides the national enforcement authority necessary to prevent deceptions on a regional or national basis. The system fails without its bipartite support—one federal, the other state.

It has been forty years since the Wheeler Lea amendement was passed, specifically adding deception as a prohibited practice. We have today a firm body of precedent in both state and federal courts defining the meaning of the term. Years of unnecessary litigation stand before us if the amendments are adopted. This litigation is a significant cost for both state governments, not to mention defendant businesses. This Committee should impose a heavy burden of proof on proponents of such change.

The current law of deception is not vague and unclear. A representation is deceptive if it has the tendency to mislead unsophisticated consumers. Advertisements directed toward vulnerable consumers are given close scrutiny. Such vulnerable consumers include those suffering from disease, those with a lack of education, or who have low income, or are naive, or who are in a member of a minority group.[15] The meaning of deceptive is defined by judicial precedent, a substantial and building body of state law, and perhaps one-half of the 70 volumes of FTC decisions since 1938. For most instances, there is a case on point. The states do not find the idea that the law is unclear to be credible. Any change of the section 5(a), no matter how clear it is supposed to be, cannot compete with the clarity of such a thorough body of precedent. Certainly the proposals at hand will dreadfully increase the ambiguity.

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[11] National Consumer Law Center, Unfair and Deceptive Acts and Practices § 1.3.3, p. 7 (1982).

[12] National Consumer Law Center, *Unfair and Deceptive Acts and Practices* (1981) p. 21.

[13] Ala. Code § 8-19-6; Alaska Stat. § 45.50.545; Ariz. Rev. Stat. Ann. § 44-1522(B); Conn. Gen. Stat. § 42-110(B); Fla. Stat. Ann. § 501.204 (West); Ga. Code Ann. § 106-1201; Hawaii Rev. Stat. § 480-3; Idaho Code § 604; Me. Rev. Stat. Ann. tit. 5, § 207(1); Md. Com. Law Code Ann. § 13-105; Mass. Gen. Laws Ann. ch. 93A, § 2(b) (West); Mont. Rev. Codes Ann. § 85-403; N.H. Rev. Stat. Am. § 358-A-13; N.M. Stat. Ann. § 49-15-4; R.I. Gen. Laws § 6-13.1-3; S.C. Code § 66-71.1; Tenn. Code Ann. § 47-18-115; Utah Code Ann. § 13-11-4; Vt. Stat. Ann. tit. 9, § 2453; W.Va. § 46A-6-103. The language is, typically, "It is the intent of the legislature that in construing . . . this Act the courts will be guided by interpretations given by the Federal Trade Commission and the federal courts to Section 5(a)(1) of the Federal Trade Commissioin Act."

[14] *See, State* v. *Marsden,* Clearinghouse No. 27,048 (Alaska Super Ct 1977); *People ex rel Nelson* v. *Superior Court* (Kempton) 20 Ariz App 591,514 P. 2d 1042 (1973); *People ex rel. Dunbar* v. *Gym of America, Inc.* 177 Colo. 97, 493 P. 2d 660, Pov L Rep (CCH) 15,517 (1972); *Fitzgerald* v. *Chicago Title and Trust Co.* 46 Ill.App.3d 526, 361 N.E.2d 94, 5 Ill. Dec. 94 (1977) *Gour* v. *Daray Motors,* 373 So.2d 571 (La.Ct.App.1979); *State ex rel Gusie* v. *Alaska Overseas, Inc.* No. 8718, Clearinghouse No. 26,203 (La.Ct.App. Oct. 12, 1977); *Schubach* v. *Household Finance Corp.* 375 Mass. 133, 376 N.E.2d 140, 12 Clearinghouse Rev. 119 (No. 2) Clearinghouse No. 20,318 (1976); *Nader* v. *Citron,* 372 Mass. 96, 360 N.E.2d 870 (1977); *PMP Associates, Inc.* v. *Globe Newspaper Co.,* 366 Mass. 593, 322 N.E.2d 915 (1975); *Slaney* v. *Westwood Auto Inc.,* 366 Mass. 688, 322 N.E.2d 768 (1975); *Commonwealth* v. *Decotis,* 366 Mass. 234, 316 N.E.2d 748 (1974); *People ex rel Lefkowitz* v. *Colorado State Christian College,* 76 Misc.2d 50, 346 N.Y.S.2d 482 (Sup Ct 1973); *Hardy* v. *Toler,* 288 N.C. 303, 218 S.E.2d 342 (1975); *Thomas* v. *Sun Furniture and Applicance Co.,* 61 Ohio App.2d 78, 399 N.E.2d 567, 11 Ohio Op.3d 26 (1978); *Santiago* v. *Kresge Co.,* 2 Ohio Op.3d 54 (C.P. Cuyahoga Cty 1976); *Commonwealth* v. *Flick,* No. 1717 CD 1976 Clearinghouse No. 26,032 (Pa. Commw. Ct. Feb. 10, 1978); *Americans Be Independent* v. *Commonwealth,* 14 Pa. Commw. Ct 179, 321 A.2d 721 (1974); *Commonwealth* v. *Hush-Tone Industries, Inc.,* No. 305 CD 1970 Clearinghouse No. 26,025 (Pa. Commw. Ct. Dec. 22, 1971). *Commonwealth* v. *Handicapped Industries, Inc.,* No. 74-11131-09-5, Clearinghouse No. 26,027 (Bucks Cty, Pa. Nov. 20, 1977); *Commonwealth* v. *Programmed Learning Systems, Inc.,* No. 1936 Oct. 1974, Clearinghouse No. 26,019 (CP Allegheny Cty, Pa. Nov. 20, 1975); *Commonwealth* v. *Empire Express Inc.* 28 Erie County L.J. 27, Clearinghouse No. 11,129 (CP Erie Cty. Pa. 1972); *Commonwealth* v. *Gold Bond Industries, Inc.* No. 562 April Term 1972, Clearinghouse No. 26208 (CP Allegheny Cty, Pa. Apr. 26, 1972); *State* v. *Credit Bureau of Laredo,* 530 S.W.2d 288 (Tex. 1975); *Sprading* v. *Williams,* 553 S.W.2d 143 (Tex. Civ. App. 1977); *Wesware Inc.* v. *State,* 488 S.W.2d 844 (Tex. Civ. App. 1972); *State* v. *Packard,* No. C242-74WrC, Clearinghouse No. 27,066 (Vt. Super.Ct. May 5, 1977); *Lightfoot* v. *McDonald,* 86 Wash.2d331,544 P.2d 88 (1976); *Testo* v. *Russ Dunmire Oldsmobile Inc.,* 16 Wash.App. 39,554 P.2d 349, Pov. L. Rep. (CCH) 23,503 (1976) But see *State ex rel Edminston* v. *J. C. Penney Co.,* 292 N.C. 311,233 S.E.2d 895, Clearinghouse No. 17,083C, Pov. L. Rep. (CCH) 24,499 (N.C. 1977); *Vargas* v. *Allied Finance Co.,* 545 S.W.2d 231 (Tex. Ct. App. 1977).

A deceptive act benefits the deceiving business, whatever its intent or the cost to the consumer. A deceptive act can be compared with common law fraud, which focuses on the intention of the seller. Common law fraud requires a false representation, made with knowledge, and intent to deceive, actually relied upon by the victim, to his damage.[16] Common law fraud focuses on the intention of the seller. In essence, the seller must be culpable, guility of a quasi-criminal intention to be liable. The seller may deceive consumers, and profit from the deception, as long as proof of one element is lacking.[17] While these elements may be an appropriate standard for criminal law or punitive damages, it has long since ceased to be the standard of recovery for misrepresentations in consumer transactions. Innocent but express misrepresentations can be the basis for recovery, even at common law. The FTC Act is designed to prevent deceptive representations from being a factor in the marketplace.

Unlike common law fraud, a deceptive practice does not focus on the intention of the seller, but takes notice that, whatever the intent, the seller may profit from a deceptive practice. Hence, the fact of the practice—whether it is deceptive—is the focus of the inquiry. Deception does not require evil intent, negligence, or some other indicia of culpability on the seller's part. Nor does it require proof of the quality of the consumer—whether the deceived consumer is of average intelligence or not, or the nature of the injury to the consumer or the business community. It is sufficient that the practice is deceptive. A deceptive act is not necessarily a false statement of fact. The definition recognizes that the marketplace contains consumers sophisticated and unsophisticated, the brilliant and the ignorant. To be deceptive the act need only have the tendency or capacity to deceive even gullible and unsophisticated consumers. The state statutes are expensively and liberally construed to protect consumers against deceptive practices.

II. THE PROPOSED AMENDMENTS ARE AN INEFFICIENT APPROACH WITH CONSIDERABLE AND UNNECESSARY COSTS TO BE BORN BY THE STATE

The proposed changes to the FTC act come in a variety of proposals, most of which are more ambiguous than the well-defined law that has evolved over the last forty years. All proposed changes entail severe costs for the states' efforts to enforce their statutes:

1. Unnecessary amendment of State statutes. The proposals, if adopted, could effectively amend state statutes, by state judicial construction, since the FTC act provides both the historical basis and the body of precedent for state statutes.
2. Inefficiency. In the event FTC precedent is held to apply, additional costs of litigation accrue in all cases, even in the vast majority that are accepted as good law by Chairman Miller. States cannot afford these additional costs, which are a waste of governmental resources.
3. Costs of litigation. Even if the amendments were ultimately held inapplicable to state statutes through judicial use of FTC precedent, the states will have to litigate the question to reach that determination. Each state will have to litigate the issue.
4. Nationally lowered standards. Even if state courts universally rejected the federal changes as state precedent, the practical effect would be the same. The states cannot as a practical matter enforce their law on national advertising. The states cannot impose a higher standard of conduct on local businesses than is imposed on national advertising. Hence the standard of accepted conduct will fall to the lowest common denominator.

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[15] See, *Belmont Laboratories* v. *FTC*, 103 F.2d 538 (3d Cir. 1939); *Commonwealth* v. *Hush-Tone Industries, Inc.*, No. 305 C.D. 1970 Clearinghouse No. 26.025 (Pa. Commw. Ct. Dec. 22, 1971); *People* v. *Conway*, 42 Cal. App. 3d 875, 117 Cal. Rptr. 251 (1974); *Kugler* v. *Romain*, 58 N.J. 522, 279 A.2d 640 (1971).

[16] Restatement (Second) of Torts (1981) §§ 525–549; *Suburban Properties Management* v. *Johnson*, 236 Md. 455, 204 A.2d 326 (1964); *Broberg* v. *Mann*, 66 Ill. App. 2d 134, 213 N.E. 2d 89 (1965); *Traylor Eng. & Mfg. Co.* v. *National Container Corp.*, 70 A.2d 9 (Del. 1949).

[17] Prosser, Law of Torts p. 686 (4th ed. 1971).

We submit to this Committee that the burden of the proponents of such change has not been sustained. The premise of all of these changes is that the term is vague, gives unlimited power to the FTC to regulate advertising, and has resulted in great, unwarranted costs to consumers. Only one of the four FTC Commissioners advocates such a change. The states' attorneys general oppose the proposed change; it is unnecessary, costly and will result in meaningless additional expert testimony that adds nothing to the analysis of whether an act is deceptive. The present statutory structure of cooperation and enforcement by the states, private consumers and the FTC should not be abandoned or revised because of ambiguous and unsubstantiated claims that the benefits are insufficient.

First, statutory interpretations of the state statutes will inevitably be affected by federal precedent. Virtually all state statutes prohibit deceptive acts, in general language. The Federal Act provides not only the historical basis for the state acts, but also the great bulk of precedent for the states. The history of the FTC Act and state legislative acceptance of its principals is almost unique in federal/state cooperative efforts. By normal rules of statutory construction, federal precedent is and will be the basis of state judicial construction. 2A Sutherland Statutory Construction, § 52.02, p. 329 (Sands ed. 1973). In fact, over 20 state statutes explicitly declare that "it is the intent of the legislature that in construing . . . this act the courts will be guided by the interpretations given by the Federal Trade Commission and the Federal Courts to Section 5(a)(1) of the Federal Trade Commission Act." [18]

Rarely can a stronger historical basis be found for construing the state statutes consistent with the federal precedent. The impact will be dramatic, and will occur almost contemporaneously with the emergence of new federal precedent. As a matter of statutory construction, many states will follow the federal precedent. Each state will have to litigate the extent to which its state will be guided by the federal definitions. While state courts may technically have the power not to follow federal precedent, that argument begs the question, and in essence abandons the supposed need of legislatures to adopt the rule as to deceptive. Many, perhaps, most states' courts will follow federal precedent. It is certainly irrelevant to note that such new federal precedent cannot be used until it is created, sometime in the future. Such an argument only underscores the long-term litigation that the amendment would create.

Second, at least 50 states, and at least as many businesses, will litigate the question. Is the cost of this litigation necessary? The attorneys general believe it is completely unwarranted.

Third, in the states where federal precedent is held binding, the states will bear additional litigation costs. The states believe the additional required proof provide nothing further in probative value.

Fourth and finally, the question of whether all or most of the states will feel bound by federal precedent is really a moot issue in considering what standards the states will apply. The states have no choice but to apply the standards used by the FTC Act, for states cannot effectively impose state standards on national advertising. There is a reluctance of state courts to interfere where national advertising is being distributed by a national company. State courts and state attorneys general are not equipped to prevent deceptive national advertising by national companies. An illustrative example is the recent rebate campaign by General Motors. The FTC declined any action, presumably because its cost-benefit analysis showed that rebates were a net benefit to consumers, since consumers offered rebates paid less than consumers not offered rebates. No comparison was apparently made to the effect on competitors not using deceptive pricing.

The Attorney General of Texas did not agree with the FTC's position. He decided that, under Texas law, the General Motors "Let's Get Moving" rebate program was deceptive in that it failed to disclose that twenty-five percent of the rebate cost was passed on to the dealer, who in turn frequently passed it on to the consumer; that GM used coercive tactics in threatening dealers who did not want to participate; and that GM threatened to withdraw the program without living up to its advertised claims. The case is particularly illustrative, because, as the third largest state is presumably one of the best able to impose its standards on national advertising.

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[18] This or similar language is found in the following statutes: Alaska State. § 45.50.545; Ariz. Rev. Stat. § 44-1522(B); Conn. Gen. Stat. Ann. § 42-110(b-; Fla. Stat. Ann. § 501.204; Ga. Code Ann. § 106-1201; Hawaii Rev. Stat. § 408-3; Idaho Code § 48-604; Me. Rev. Stat. tit. 5, § 207(1); Md. Com. Law Code Ann. § 13-105; Mass. Gen. Laws Ann. c. 93A § 2(b); Mont. Rev. § 49-15-4; R.I. Gen. Laws § 6-13.1-3; S.C. Code § 66-71; Tenn. Code Ann. § 47-18-115; Utah Code Ann. § 13-11-4; Vt. Stat. Ann. tit. 9, § 2453; W.Va. Code § 46A-6-103.

What happened? General Motors hired four huge law firms, that filed legal briefs beyond the physical capacity of the state's lawyers to respond. There was a brief trip to federal court. The lawsuit is still pending, but in the interim General Motors apparently decided to punish the state of Texas in a way that became a campaign liability for Attorney General Mark White. General Motors refused to offer the terms of its next incentive program, lower interest rates, to Texas residents, reportedly directing inquiries to the Texas Attorney General. In essence, Texas was told to live with deceptive pricing, or get no price reductions. The lesson, well understood by other states, is that no state can realistically enforce its state law effectively on a national advertising campaign by a national company. Whether or not FTC precedent is legally binding on the states, it is de facto binding. Earlier cutbacks in the FTC have already had an effect on the states' ability to prevent deceptive trade practices. In the event that Congress amends the FTC Act, we will again see the federal government dictating unwanted standards to the states.

This example shows that the FTC sets the national standards; [19] advertising practices will inevitably fall to the lowest common denominator. National advertising constitutes 55% of all advertising.[20] It sets the tone and the ethic of all advertising, local and national. No state can effectively enforce higher state standards on national advertising campaigns. The federal standard, which is the national standard, inherently become the state standard. Once this fact becomes apparent, the states will be unable to enforce existing and accepted state standards on local advertising that comports with the reduced federal standards, but that flunks the state standards.

III. THE PROPOSALS WOULD ADD NEW AMBIGUITIES, AND UNNECESSARY ELEMENTS OF PROOF, AND CONSIDERABLE COSTS OF LITIGATION THAT WILL BE BORNE BY THE STATES

A. A lack of need for fundamental changes.—When this Committee considers amending 44 years of precedent, we think it only appropriate to ask what advantages do the proposals have over existing law? What difficulties will the states have under this proposed law?

The claimed advances are indeed obscure. We are confronted with a series of proposals, the most important of which, Chairman Miller's proposal, has not even been reduced to bill form.

Chairman Miller offers several reasons for such a statutory amendment: (1) accountability to the legislative process, (2) to offer guidance to the FTC in ordering its priorities, since it is faced with "near limitless possibilities of cases to bring"; (3) in the event Congress limits the definition of "unfairness," to prevent extension of the FTC's jurisdiction over "deceptive" acts to defeat the Congressional purpose.[21] Chairman Miller further suggests that consumers have been harmed by the existing standards, [22] a case he wholly fails to make.

The FTC has been closely scrutinized by Congress in these and previous proceedings, such as the recent action in the Congressional veto of the proposed "used car" rule indicates. In the event there are specific issues that the Congress disagrees with, the issues should be dealt with in specifics, not by an overall restructuring of the law, which will effect all cases, good law and bad law alike.

Congressional action should be confined to specific issues. Or, the Congress could place in the reauthorization act a statement of priorities for the FTC. Certainly, such a directed statement is better designed to meet the issues Chairman Miller raises, rather than a basic restructuring of such a basic source of law for the country. Such guidance could also be made an internal FTC procedure by regulation, similar to internal procedures which govern the Internal Revenue Service, an agency with perhaps even a broader range of cases from which to set priorities. Directed Congressional guidance has the advantage of setting actual priorities by definite standards, without adding costs to enforcement of all cases, affecting the underlying precedent of the FTC, and causing difficulties and unwanted financial burdens to the states.

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[19] The states have attempted to address this problem by regional cooperation, but with considerable duplication of effort. In the Northeast, four states including Vermont have filed a civil action against Suburu, the Japanese car manufacturer, over a defect in a front wheel rubber boot which costs consumers $400-500 in preventable repairs when the defect appears. Each of the complaining states must litigate its case in its state court. Suburu must of course defend in each state.

[20] U.S. Department of Commerce, Statistical Abstract of the United States—1981, p. 572.

[21] Separate Statement of James C. Miller III, Chairman, FTC, before the Subcommittee on Commerce, Transportation and Tourism, Committee on Energy and Commerce, U.S. House of Representatives.

[22] *Id.* at 7.

Chairman Miller's last concern, which is not explained, could just as effectively be addressed through either of the foregoing methods, if it is necessary to address it at all. It seems appropriate to request clarification of just how the definition of deceptive is going to be applied to unfairness jurisdiction.

Chairman Miller does propose another means of meeting his concerns—fundamental changes in the FTC Act. We unfortunately lack a specific legislative proposal—certainly a necessary antecedent to the states' fair opportunity to comment on the proposal. But Chairman Miller does offer us a suggestion of the proposal.

First, he would require for an act or practice to be deceptive that there be demonstrable "consumer injury." He asserts that if a product is cheap, then consumers led to its purchase will not buy it again.

Secondly, he proposes that the Congress define deceptive to include a reasonableness standard, referring to a standard of the reasonable consumer.[23] But he agrees that reasonableness depends upon the circumstances, the age, sophistication and vulnerability of the intended audience of an advertisement. Further, for vulnerable groups, he offers an alternative standard, if the "perpetrator knew, or should have known, that some consumers would be misled." [24]

Third, all opinions would be exempt, no matter how misleading, exaggerated or simply inaccurate.

The attorneys general have great difficulty with these proposed standards. First and foremost, we are not troubled by the claims of ambiguity in the current law. We disagree as to the ambiguity, and submit that the proposals multiply any claimed ambiguity, for they commence without the valuable body of 44 years of precedent for the current law. Any lawyer knows that new litigation will have to be clarified through hearings and litigation; while this may be good for lawyers, it is costly both to 51 governments and more defendants.

B. A lack of analysis.—The proposals have additional defects:

1. The supporting analysis by Timothy J. Muris limits its consideration of injury to the effect of the deception on the consumer in the particular transaction, ignoring the other economic (and social) effects of permitting deceptive practices in the marketplace.[25]

2. The analysis does not actually demonstrate the use of cost-benefit analysis in a particular transaction, and in fact avoids it in supposedly "clear" cases that are in fact indistinguishable from cases seen to lack merit. The analysis does not demonstrate any recognizable rule as to when extrinsic evidence is not required. The analysis therefore does not demonstrate that the institutionalization of expert testimony and surveys that would result would accomplish much if anything.

3. The cost-benefit analysis is not applied to the proposed amendments: Is it cost-beneficial for the government to demand costly economic impact studies in all cases, when a few cases from many volumes of cases are criticized as being in error?

4. The standard of reasonableness—the "reasonable consumer"—has not been thoughtfully addressed. It is most unclear how this standard is likely to correct claimed problems with the current statute.

C. Significant additional costs are not included in the cost-benefit analysis.—The "cost-benefit" or consumer injury analysis—that the FTC's intervention into the free market may not be cost efficient, and has not resulted always in a net benefit to consumers—underlies much of the proposed change. In short, the claim is that proposed "cost-benefit" analysis is inherently more efficient, because it requires each case to be justified on its facts. The statute will become self-righting, and not subject to the wasteful use of governmental resources.

The claim is unsupported in three important respects: Mr. Muris inappropriately confines analysis of the injury from deception. First, he confines the analysis to injury to the consumer, i.e. if the consumer gets a good product for a similar price, without undue waste of time, there is no injury. To confine analysis to the consumer is to ignore the significant costs to businesses that do not engage in deceptive practices. The predictable result is that if there is economic advantage to be gained from the initial deception, but the consumer gets as much or better from the transaction than if he had shopped next door, there is no injury. This confining analysis ignores the damage to other businesses, to business practices generally, and to the level of information which the consumer can expect in the marketplace. Deceptive practices would be allowed as long as there was no demonstrable injury to be particular consumer in the transaction.

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[23] Id at 9-13.

[24] Id at 12.

[25] Id. at 76-77.

Not considered is the price of honesty. What social value do we place on honesty in trade practices? There is certainly a great social cost in encouraging or allowing the disemination of deceptive information in the marketplace. Do we really want to change our laws to permit business to profit from deceptive practices?

Not considered either is the reduction of accurate information in the marketplaces. It is not rational for us to expect, for instance, that consumers can research and try the 10,000 to 15,000 different products that confront consumers when they walk into a supermarket. The information about the products will come from the marketplace. Businesses spent $54 billion on advertising in 1980.[26] There is no social or economic utility in allowing competition on inaccurate statements or opinions.

Nor should businesses be placed in a posture where they must use deceptive claims in order to compete. Honest businesses deserve not to be preyed upon by those businesses who would use deceptive trade practices in the marketplace. If deceptive practices are effective,[27] and if the consumer cannot demonstrate injury,[28] the economic benefit goes to the business employing the deception. Chairman Miller would analyze only the actual cost to the consumer from the deception in that transaction, as compared to the same transaction without the deception.

D. The "injury" analysis is incapable of ready application.—Commissioner Miller's analysis confines itself to the "cost" to the consumer at the point of purchase. The analysis thereby ignores one of the basic techniques of consumer frauds, and thus the basic concern of consumer protection law—the initial deceptive contact, by which a business can identify interested customers.

The analysis of Chairman Miller and Mr. Muris reaches opposite conclusions from essentially indistinguishable cases where there were initially deceptive contacts. The low level of proof on non-economic injury that he is willing to accept in some cases is not allowed in others. We are in essence left with no articulated standard.

In the *Sears* case,[29] where Sears falsely claimed its dishwasher would clean without scraping or rinsing, Mr. Muris would accept as sufficient proof that the product commanded a premium price.[30] But even here, the problems are not easy. What if the manufacturer attributed the premium to a better motor? What if the dishwasher sold for the same or less as its competitors machines, with equal ability to clean? Where would be the injury, except to competitors who had lost sales of products not associated with deceptive claims? Is any cost associated with most dishwasher manufacturers making false claims? Moreover a survey to establishing that consumers would value such a product more highly tells us only what the advertiser knew when he chose the ad's claim. If consumers did not value the quality, it would not be advertised.

The criticized Poli-Grip example,[31] is essentially indistinguishable from the priased *Sears* case, except that Poli-grip is cheaper and most denture competitors resorted to similarly false claims.[32] In denture creams, the consumer had a host of falsehoods from which to choose. How does one value that damage? In fact, in that case, it was reasonable for the consumer to believe that the best (false) claims indicated the best gripping if nonetheless imperfect product. Thus the market deteriorated into a host of deceptive claims. Competitors met their competition. The end result was simply a devotion of the advertising to the dissemination of falsehood. Is there no social or economic cost?

Chairman Miller claims he would maintain "bait and switch" law, but it is not clear how. The injury from bait and switch is essentially indistinguishable from the injury from deceptive pricing, which the Chairman does not consider injurious.[33] In a bait and switch fraud, the consumer is attracted to a product and dealer by a low price, which is subsequently disparaged as of low quality. The consumer is then switched to a higher priced product, that may well be a good value. Mr. Muris finds the injury of driving across town sufficient in bait and switch. Indistinquishable is deceptive pricing, where the consumer is attracted by a significant discount for a product that he is told normally sells for much more. He buys the product, thinking it is a better value and presumably of higher quality than it really is. He has been deceived in a matter directly relating to the quality of the product he actually purchased.

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[26] U.S. Dept. of Commerce, Statistical Abstract of the United States—1981, p. 572.

[27] Presumably deceptive practices would not be a problem if they were not effective, i.e., cost-beneficial.

[28] Or if, due to the additional burden of proof, the FTC or the state has not yet completed its economic analysis.

[29] Sears, Roebuck & Co., 95 F.T.C. 406, 416–419 (1980).

[30] U.S. Senate, Hearings before the Committee on Commerce, Science, and Transportation on Reauthorization of the Federal Trade Commission, March 18 and 19, 1982, Serial No. 97-108, pp. 78, 82.

[31] Block Drug Company, 90 F.T.C. 893 (1977).

[32] The advertising apparently paid off, since it continued. The profit to be made from the deceptive claim which appeared inconceivable to the dissenting FTC commissioner was apparently a reality in the marketplace.

[33] See U.S. Senate, Hearings before the Committee on Commerce, Science, and Transportation on Reauthorization of the Federal Trade Commission, March 18 and 19, 1982, Serial No. 97-108, pp. 78–79.

In both bait and switch, and deceptive pricing, the consumer was initially attracted to buy the product by a claim.[34] In the bait and switch case, when the consumer bought the higher-priced product, he may have gotten exactly what he believed he was getting. In the phony discount case, he got something less. The point of either case is that the business used false claims to attract sales.

False claims do indeed attract consumers—why else would the claims be made. If false claims are permitted, as long as the merchandise is as good a value as the competition, then all competing businesses must compete, probably with false claims. In essence, Chairman Miller is reinstating the common law elements of fraud—reliance and actual damages. If deception is permissible absent damages, the market will deteriorate, since false claims are permissible. The consumer is fed false information. Those businesses who refuse to make deceptive claims may lose business, but their losses, not being consumer losses, are not considered.[35] My office in Vermont is currently investigating a deceptive pricing case in which the offending business—a furniture store—appears to have done its normal annual volume of business in 90 days—business that it has essentially stolen from the competing business, which has not engaged in deceptive pricing. Yet such conduct is apparently tolerated under the proposal.

Coupled with the assertion that misleading or inaccurate opinions should never be considered deceptive, Commissioner Miller's proposal would carve out a large exemption for deceptive claims. There is no social or economic purpose to be served by such an exemption. False claims are an economic waste. Such claims flood consumers with false information, reducing the credibility of all advertising, a $54 billion industry in 1980, taking money from the pockets of more scrupulous businesses, and reducing the efficiency of the marketplace.

Commissioner Miller has failed to indicate how the required proof of injury will operate an actual case. There has been no thorough economic analysis of the effect in any one case. Furthermore, by confining the inquiry to the transaction itself, Commissioner Miller ignores the effect on the market, or on competitors and their behavior, or on subsequent transactions. No thorough economic analysis has been illustrated even in one case, and yet this Committee is being asked to institutionalize such analyses in all FTC cases. Under this proposal we would embark upon a battle of the experts, who would probably be able to show injury or lack of injury, depending upon who hired them.

The state attorneys general are doubtful that such an expert or survey testimony will add anything to our cases except expense. Since this Committee is being told that it would, perhaps the first cost-benefit analysis should be of the proposal, to see whether institutionalizing this kind of testimony by an Act of Congress will in fact save governmental funds, increase fairness of the result, or both. Remember that this testimony will in fact be required not just in the cases Mr. Miller finds to be "mistakes," but in all cases, of which these supposed "mistakes" are but a small percentage from 70 volumes of FTC law since 1938.[36] Thus the amendment would have an inherent inefficiency, by building in costs of litigation, for both the government and the defendant, in cases that the proposal does not take aim. Let us begin our first cost-benefit analysis by finding the costs of such studies and such testimony before we require it in all cases, and unwittingly require it of fifty states.

Any cost-benefit of the proposals should demonstrate that there will be a savings in net governmental and business resources, not simply that a particular case would not be brought. The study should include not only costs incurred at the FTC, but the states as well. More efficient government and greater economic efficiency should always be the goal, but simple assertions of efficiency are meaningless. A consideration of net state and federal impact is a fair and minimal request. Remember that this the proposal will institutionalize expert economic testimony and consumer surveys in essentially all cases.[37]

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[34] Vermont has clear regulations on deceptive pricing, consistent with the supposedly mistaken ruling in the *Levitz Furniture* case. Vermont Reg. Ann. CF 110; see, Levitz Furniture Corporation, 88 F.T.C. 263 (1976), and bait and switch tactics. Vermont Reg. Ann. CF 103.01. (See Appendix C.) One or both regulation, which are self-explanatory and accepted parts of Vermont business ethics, would be jeopardized by the proposed amendment to the definition of "deceptive."

[35] U.S. Senate, Hearings before the Committee on Commerce, Science, and Transportation on Reauthorization of the Federal Trade Commission, March 18 and 19, 1982, Serial No. 97-108, p. 77.

[36] While I have not counted, perhaps deal with unfair and deceptive acts.

The attorneys general of the states do not feel either they or their opponents can afford such costs, and do not believe that a "battle of the experts" will contribute any efficiency to the process or to the result. Experts can be hired to prove most propositions. Any economic analysis of the impact of a particular deception is likely to involve conflicting testimony of the effect on the market. For a great expenditure of resources we will be presented a volume of economic testimony that is essentially irrelevant to the underlying point—whether the claim is deceptive. If the states cannot afford such a waste of money, perhaps the federal government should ask why it is able to afford such an ongoing cost.

E. The "reasonable consumer" standard does not advance the analysis.—Though it sounds reasonable, the reasonable consumer, or "consumer acting reasonably" standard contributes nothing to the analysis at hand.

The test is almost wholly unapplied by the Chairman or Mr. Muris. He states that an act or practice should be deceptive "only if likely to mislead individuals acting reasonably under the circumstances."[38] Currently, a deceptive act can be one that misleads the unthinking, the ignorant, or the credulous.[39]

The initial question is, in a broad market, who is a reasonable consumer. If we choose a person of average intelligence, then we have eliminated roughly half the population. In essence, we begin to repeat the analysis of the courts and the FTC. If we are to protect people beyond those of above average intelligence, we must begin to think of the below-average consumer.

Perhaps an ignorant and unsophisticated consumer should be considered to be a member of a vulnerable group. Businesses can just as easily profit from deceiving the vulnerable. Oddly enough, for a vulnerable group, Commissioner Miller proposes a higher standard of proof. Whereas with an average consumer acting reasonably, no intent on the part of the deceiver must be shown, if the victim is a member of a vulnerable group (hence presumably more gullible and likely to be the victim of a deception), then the FTC must show that the "perpetrator knew, or should have known, that some consumers would be misled."[40]

This requirement of knowledge of the result is enough from which to infer intent, i.e. common law fraud. Hence, for vulnerable groups, who presumably need the most protection, the proposal imposes a higher standard of proof—knowledge—than exists for the less vulnerable "reasonable consumer." In essence, a common law fraud requirement would be required where the victim is more in need of protection. If business deceives and injures an elderly woman with a cancer "cure," the proposal requires knowledge, This is indeed a topsy-turvy approach to consumer protection.

An example from Vermont is a business called the "Herbal Education Center," a small order firm operating out of Vermont that bilked consumers nation-wide. I would concede that the consumers were unsophisticated, credulous and gullible. The Herbal Educational Center attributed miraculous qualities to common herbs; other, dangerous herbs were also claimed to have curative qualities. On its cover was a quotation from the Old Testament. Perhaps in 1982, it is difficult for use to believe that even the unsophisticated would believe that cayenne pepper, for instance, is a

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[37] In most state proceedings, such surveys would be inadmissible hearsay unless accompanied by strong and convincing expert testimony that the surveys were accurately reflecting the views of consumers. Hearsay is inadmissible because it has such a low probative value. Is such testimony upon which our courts look askance as unreliable, really going to add anything to the proceedings?

[38] U.S. Senate, Hearings before the Committee on Commerce, Science, and Transportation on Reauthorization of the Federal Trade Commission, March 18 and 19, 1982, Serial No. 97-108, p. 63.

[39] *FTC* v. *Standard Education Society,* 302 U.S. 112 (1937); *Standard Oil of California* v. *FTC,* 577 F. 2d 653 (9th Cir. 1978); *Staufer Laboratories, Inc.* v. *FTC,* 343 F. 2d 75 (9th Cir. 1978); *FTC* v. *Sterling Drug Inc.,* 317 F. 2d 669 (2d Cir. 1963); *Charles of the Ritz Distributing Co.* v. *FTC,* 143 F. 2d 676 (2d Cir. 1944); *People ex rel Lefkowitz* v. *Volkswagen of America,* 366 N.Y.S. 2d 157 (1975).

[40] Separate Statement of James C. Miller III, Chairman, FTC, before Subcommittee on Commerce, Transportation and Tourism, Committee on Energy and Commerce, U.S. House of Representatives. April 1, 1982, p. 12.

"miracle herb" curing "all forms of low diseases," as claimed. Yet it is difficult not to sympahize with the victims. As one woman wrote:

"Their catalogue is full of scripture. Yet they took my money knowing they were in financial trouble I am sure.

"I am a senior citizen and my money means much to me. I do not like to be taken by people posing as Christians or any others.

"I do not know whether you can help me with this. I will appreciate your help."

Our office was able to help. By moving swiftly, we were able to recover $180,000 for the estimated 9,000 victims. We did not have to concern ourselves with whether the victims were acting reasonably, or whether they were members of a vulnerable group. Under Chairman Miller's proposal, the state of Vermont might have to prove the seller's knowledge that the herbs did not cure. I can tell you quite frankly, my office does not have the number of people needed to find knowledge of this or any business. This is an intolerable burden for this Committee to impose on the states. It would make protection of the most vulnerable people the most difficult, and could entail long delays and much greater costs on the few cases that were brought.

Lastly, I do not know whether or not the consumers who bought from Herbal Education were reasonable or not under Chairman Miller's definition. I am not sure what a demographic profile of the thousands of customers would reveal. Such an inquiry is irrelevant to the underlying issue of deception. Furthermore, if the answer on such a distinct set of facts is unclear, I see no prospect that these amendments will perform as claimed to clarify the law.

IV. CONCLUSION

On behalf of the attorneys general of the states, I urge the Committee to reject these proposals. They are poorly conceived, incapable of ready application, and a giant step backward from the joint efforts of the federal government and the states to eliminate deception in the marketplace.

In the event this Committee wishes to pursue such proposals further, they should be given the thorough study and scholarly analysis appropriate to such a major change in law, similar to that undertaken by restatements of the law. This Committee should not accept the unsubstantiated claim that the FTC needs major revision. It should demand proof. The attorneys general do not believe that the definition of "deception," developed through forty-four years of experience, needs revision. The National Association of Attorneys General and the attorneys general would volunteer to assist this Committee into an inquiry of the efficacy of the FTC and the state mini-FTC acts.

APPENDIX A

NATIONAL ASSOCIATION OF ATTORNEYS GENERAL—JULY 18, 1982

RESOLUTION.—FTC AUTHORIZATION

Whereas, the Congress is considering amendments to Section 5(a) of the Federal Trade Commission Act, which would change the FTC's jurisdiction; and

Whereas, such amendments include the codification of cost-benefit analysis, which is an appropriate policy making tool in the development of unfairness cases but is unnecessarily restrictive as the standard to be used in all cases, and various restrictive and unwarranted changes in the definition of deception; and

Whereas, an amendment providing an exemption for commercial speech beyond the First Amendment exemption is unnecessary in light of the existence of a well developed body of case law that has already resolved this issue; and

Whereas, virtually every state prohibits deceptive practices and approximately 30 states also prohibit unfair and deceptive acts or practices; and

Whereas, 20 state statutes explicitly say state courts should follow Commission and federal court interpretations of the FTC Act and where statutes do not contain this explicit directive, most state courts have interpreted state statutes consistently with the FTC Act; and

Whereas, these changes were initially proposed without consultation with state officials: Now, therefore,

Be it resolved, That the National Association of Attorneys General:

1. Opposes any amendments to Section 5(a) of the FTC Act that might circumscribe the scope of consumer protection statutes at the state level and would undermine the ability of states to protect their citizens; and

2. Urges the Congress that it if wishes to amend the FTC Act in such a way that will impact on state law, these changes should be subject to extensive study and

consultation with state govornors, legislators, and attorneys general prior to enactment.

3. Authorizes the President of the Association to appoint an ad hoc committee to monitor legislative developments and make recommendations to the Association regarding any additional proposed amendments to Section 5 of the Federal Trade Commission Act.

4. Authorizes its General Counsel to transmit these views to the appropriate members of the Administration and Congress.

APPENDIX B

TABLE OF STATE STATUTES

[State Deceptive Practices Acts]

Jurisdiction and Statutory Cities (et seq.)	All § 5 prohibitions	Unfair or deceptive practices	Deceptive practices	Private actions
Alabama.—Alabama Code Title B § 19-1			X	X
Alaska.—Alaska Statute § 45.50.471	X		X	X
Arizona.—Arizona Revised Statute § 44-1521			X	
Arkansas.—Arkansas Statute Annotated § 70-901			X	
California.—California Civil Code § 3369 (Deering); California Business and Professional Code § 17500 (Deering).		X	X	X
Colorado.—Colorado Revised Statute § 6-1-102			X	X
Connecticut.—Connecticut General Statute § 42-110	X			X
Delaware.—Delaware Codification title 6, § 25		X		
District of Columbia.—D.C. Code title 28 App. § 1		X	X	X
Florida.—Florida Statute § 501.201	X			X
Georgia.—Georgia Code § 106.1210		X	X	X
Hawaii.—Hawaii Revised Statute § 481A	X			X
Idaho.[1]—Idaho Code § 48-601	X		X	X
Illinois.—Illinois Revised Statute chapter 121½, § 261	X			X
Indiana.—Indiana Code § 24-5-0.5			X	
Iowa.—Iowa Code § 713-24			X	
Kansas.—Kansas Statute § 50-623			X	X
Kentucky.[2]—Kentucky Revised Statute § 367.110		X		
Louisiana.—Louisiana Revised Statute Annotated § 51:1401 (West)	X			X
Maine.—Maine Revised Statute title 5, § 206	X			X
Maryland.—Maryland Commonwealth Law Annotated § 13-101		X	X	X
Massachusetts.—Massachusetts General Laws Annotated chapter 93A	X			X
Michigan.—Michigan Composition Laws § 445.901		X	X	X
Minnesota.—Minnesota Statute Annotated § 325.771			X	X
Mississippi.[3]—Mississippi Code Annotated § 75-24-1	X		X	X
Missouri.—Missouri Annotated Statute § 407.010			X	X
Montana.—Montana Revised Codes Annotated § 85-401	X			X
Nebraska.—Nebraska Revised Statute § 59-1601	X			X
Nevada.—Nevada Revised Statute § 598-360			X	
New Hampshire.—New Hampshire Revised Statute Annotated § 358-A:1.	X		X	X
New Jersey.—New Jersey Statute Annotated § 56:8-1 (West)			X	X
New Mexico.—New Mexico Statute Annotated § 49-15-1		X	X	X
New York.—New York General Business Law § 349 (McKinney)			X	
North Carolina.—North Carolina General Statute and 75-1	X			X
North Dakota.—North Dakota Central Code § 51-15-01			X	
Ohio.—Ohio Revised Code Annotated § 1345.01 (Page)		X	X	X
Oklahoma.—Oklahoma Statute Annotated Title 15, § 751 (West)			X	
Oregon.—Oregon Revised Statute § 646.605		X	X	X
Pennsylvania.—Pennsylvania Statute Annotated title 73, § 201-1 (Purdon).	X		X	X
Rhode Island.—Rhode Island General Laws § 6-13.1-1	X		X	X
South Carolina.—South Carolina Code § 39-5-10	X			X
South Dakota.—South Dakota Complied Laws Annotated § 37-24-1			X	X
Tennessee.—Tennessee Code Annotated title 47-18		X	X	X
Texas.—Texas Business and Commission Code Annotated title 2, § 17.41 (Vernon).			X	X
Utah.—Utah Code Annotated § 13-11-1			X	X

Footnotes at end of table.

TABLE OF STATE STATUTES—Continued

[State Deceptive Practices Acts]

Jurisdiction and Statutory Cites (et seq.)	All § 5 prohibitions	Unfair or deceptive practices	Deceptive practices	Private actions
Vermont.—Vermont Statute Annotated title 9, § 2451(a)	X			X
Virginia.—Virginia Code § 59.1-196			X	X
Washington.—Washington Revised Code § 19.86.010	X			X
West Virginia.—West Virginia Code § 46A-6-101	X		X	X
Wisconsin.—Wisconsin Statute Annotated § 100.20	X			X
Wyoming.—Wyoming Statute § 40-102			X	X

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[1] While the Idaho statute is substantially similar, it differs in some respects, including but not limited to a requirement in certain instances of knowledge, actual or implied, of the commission of one of the prohibited acts or practices.

[2] Note that the Kentucky statute includes a provision that the act be unconscionable in addition to unfair.

[3] The Mississippi statute differs substantially from Section 5(a) in that it makes illegal only certain specific acts or practices.

APPENDIX C

VERMONT REGULATION: DECEPTIVE PRICING

CF 110.01 Prohibited acts.—It shall constitute an unfair and deceptive trade act and practice in commerce under 9 V.S.A. section 24539(a) for a seller or solicitor to solicit purchases of goods or services through the use of former price comparisons, retail price comparisons, comparable value comparisons, or other miscellaneous price comparisons which are false or deceptive.

CF 110.02 Former price comparisons.—(a) A former price comparison shall be considred deceptive if the amount declared to be the former price is not the actual price at which the article was offered to the public for a reasonably substantial period of time in the recent regular course of the solicitor's business, unless an earlier time period is clearly specified;

(1) A former price is not an actual price if it is set at specific amount for the purpose of establishing a fictitious higher price on which a deceptive comparison might be based;

(2) A former price is not an actual price unless:

(A) the item was offered for sale for a reasonably substantial period of time at that price and a substantial quantity of sales were made at that price; or

(B) the item was openly offered for sale to the public for a reasonably substantial period of time, displayed in a reasonable manner, consistent with the display of items of similar type, and priced at a level established in good faith;

(b) A former price comparison shall be considered deceptive if the seller or solicitor uses the words "sale", "reduced to," or words of similar import in a solicitation when the reduction from the actual former price is less than 10 percent of the actual former price, unless the solicitation clearly specifies the actual former price and the current sales price, or clearly specifies the percentage by which the actual former price is reduced.

CF 110.03 Retail price comparisons.—(a) A retail price comparison shall be considered deceptive if the seller or solicitor declares or suggests that his sales price is a bargain price compared to other sellers in the trade area or a price which is substantially less than the prices being charged by other sellers in the trade area unless:

(1) his price is at least 5 percent lower than the price at which sustantial sales of the item are being made in the trade area; or

(2) he sets forth at the time he makes his retail price comparison both his price for the item and the price or prices being charged by the seller or sellers with whom he is comparing prices;

(b) A retail price comparison shall be considered deceptive if the sell or solicitor declares or suggests that his price is less than list price, regular price, or manufacturer's suggested price unless:

(1) A substantial number of sales of the item are being made in the trade area at the list price, regular price, or manufacturer's suggested price; or

(2) If the seller is the only person in the trade area selling the particular item, the list price, regular price, or manufacturer's suggested price meets the qualifications of an "actual former price" as defined in CF 110.02; or

(3) If the particular item has never been sold in the area, the list price is that figure at which the seller or solicitor expects to make a substantial number of sales. At the end of three months, the list price must met the qualifications of CF 110.03(b)(1) or CF 110.03(b)(2).

CF 110.04 Comparable value comparisons.—A comparable value comparison shall be considered deceptive if the seller or solicitor declares or suggests that his price or prices is a bargain price compared to the price of another item of similar grade and quality unless: (a) the other item is in fact of similar grade and quality; and (b)(1) his price is at least 5 percent lower than the price at which substantial sales of the similar item are being made in the trade area; or

(2) he sets forth at the time he makes the comparable value comparison both his price or prices and the price or prices being charged by other sellers in the trade area for the item of similar grade and quality.

CF 110.05 Miscellaneous price comparisons.—A price comparison shall be deceptive if it contains statements which declare or suggest conditions which are not true.

Examples of such deceptive price comparisons include: (a) Advertising a retail price as a wholesale price; and (b) Representing prices to be factory prices when they are not selling at the prices paid by those purchasing directly from the factory.

BAIT ADVERTISING

CF 103.01 Offers which are not bona fide.—The solicitation of consumers to purchase goods or services when the solicitation is not a bona fide effort to sell the advertised goods or services constitutes an unfair and deceptive trade act and practice in commerce under 9 V.S.A. section 2453(a).

(a) A solicitation is not bona fide when the seller or solicitor uses a statement or illustration in any advertisement which would create in the mind of a reasonable consumer a false impression of the grade, quality, quantity, make, value, model year, size, color, usability, or origin of the goods or services offered or which otherwise misrepresents the goods or services in such a manner that, on subsequent disclosure or discovery of the true facts, the consumer may be switched from the advertised goods or services to other goods or services.

(b) A solicitation is not bona fide if a seller or solicitor discourages the purchase of the advertised goods or services in order to sell other goods or services. Examples of acts or practices which usually tend to discourage the purchase of the advertised goods are:

(1) The failure to reasonably display the advertised goods at the advertised prices, if the goods are advertised for sale in a retail store;

(2) The refusal to show, demonstrate, or sell the goods or services advertised in accordance with the terms of the advertisement;

(3) Disparagement by the seller or solicitor either by acts or words of:

(A) The advertised goods or services; or

(B) The guarantee, warranty, credit terms, availability of service, repairs, or parts or any aspect of the goods or services;

(4) The showing or demonstrating of goods or services which are defective, unusable, or impractical for the purposes represented in the advertisement;

(5) The use of a sales plan or method of compensation for salesmen (or penalizing salesmen) designed to prevent or discourage them from selling the advertised goods or services;

(c) A solicitation is not bona fide if a seller or solicitor fails to have available at all outlets listed in the advertisement a sufficient quantity of the advertised goods or services at the advertised price to meet reasonably anticipated demands, unless the advertisement clearly and adequately discloses the approximately quantity of advertised goods or services available and/or that the goods or services are available only at the designated outlets;

(d) Notwithstanding the fact that a seller or solicitor does have "sufficient quantities" as described in CF 103.01(c), a solicitation is still not bona fide if the seller or solicitor refuses, after the original quantity of goods is exhausted, to take orders for the advertised goods at the advertised price during the period of the sale or, if no period is stated for a reasonble period of time after the solicitation appears, to be delivered within a reasonable period of time; provided, however, that a solicitation would be bona fide if the seller or solicitor has clearly and adequately disclosed the approximate quantity of advertised goods available or if he cannot obtain the advertised goods within a reasonable period of time at or below the former price to him.

CF 103.02 "Unselling" Advertising Goods".—In the event of sale to the consumer of the advertised goods or services, to "unsell" the consumer in conjunction with the sale or attempt to sell other higher priced goods or services in their stead contitutes an unfair and deceptive trade act and practice in commerce under 9 V.S.A. section 2453(a). Examples of acts or practices which violate CF 103.02 are:

(a) Acceptance of a deposit for the advertised goods or services, then switching of the consumer to higher priced goods or services;

(b) Failure to make delivery of the advertised goods or services, or substituted goods or services of equal or greater value, within a reasonable time, or to make a refund;

(c) Disparagement by the seller or solicitor either by acts or words of: (1) The advertised goods or services; (2) The guarantee, warranty, credit terms, availability of service, repairs, or parts, or any other aspects of the goods or services;

(d) The delivery of advertised goods or services which are defective, unusable, or impractical for the purposes represented in the advertisement in conjunction with the sale or attempts to sell other higher priced goods or services in their stead.

CF 103.03 Limitations of advertised offers.—The solicitation of consumers through written or printed advertising, promotional literature, or through radio or television advertising to purchase goods or services when the solicitation does not fully disclose any material exclusions, reservations, limitations, modifications, or conditions constitutes an unfair and deceptive trade act and practice in commerce under 9 V.S.A. section 2453(a).

(a) Examples of material exclusions, reservations, limitations, modifications, or conditions include the following:

(1) That in order to purchase the advertised goods at the advertised price, other goods must also be purchased;

(2) That the advertised goods, except in unusual circumstances, would not be capable of being picked up by the purchaser at the store, or at a storage area in reasonable close proximity to the store, on the same day that the solicitation is effective.

(b) Such material exclusions, reservations, limitations, modifications or conditions of written or printed solicitations shall be stated clearly and conspicuously in close proximity to the words stating the offer.

(c) Such material exclusions, reservations, limitations, modifications or conditions of radio or television solicitations shall be disclosed clearly in conjunction with the solicitation.

[The following information was subsequently received for the record:]

QUESTIONS OF THE COMMITTEE AND THE ANSWERS THERETO

Question 1. Could not the state attorneys general and state courts simply refuse to follow any federal changes?

Answer. It is unlikely that state courts will ignore federal precedent in the face of specific state statutes requiring that they follow it. The only possibility that states would not be bound is if the state courts construe the mandatory state statutes to apply only to FTC precedent prior to amendments. Such a course is more likely in theory than in practice. Attorneys general would probably not succeed in such an argument in many states. State courts will be very reluctant to reject federal precedent in the face of specific state statutes requiring them to abide by it.

Secondly, the prospect that state courts could reject FTC precedent is more of a theory than a practical possibility. FTC law provides the overwhelming body of precedent for judicial construction. Whatever the rule of state statutes, or the Federal intent, FTC precedent will continue to guide the states. Any changes in direction will have a significant and immediate impact on the states, and state enforcement of consumer fraud statutes.

Question 2. If the state courts did refuse to follow any federal changes, how would the states be affected?

Answer. The states will be affected as follows: first, the states would have to relitigate currently settled issues, simply to establish that they are not affected by the Federal amendment. Such a process will take years, will be costly to the states in retrying decided issues, and make it necessary to redirect a portion of their resources. This is an inefficiency and a waste of resources that states do not need in a time of national austerity.

Second, if the FTC Act loosens standards for deception in the marketplace, as a practical matter it reduces state standards as well. The states have neither the jurisdiction nor the resources to attack national deceptive practices on a state by state basis. As a result, a state would be in the untenable position of insisting on stronger state standards for deceptive practices originating locally, while national practices involving the same conduct would as a practical matter be permitted.

A dual state standard could not survive. The national standard prevails; in essence, when the federal government changes the standards unilaterally, in fact it dictates its standards to the states. At a minimum the states deserve more consultation and more study on the proposed changes, before such unilateral action by the federal government. The states see nothing seriously wrong with the present standard of deception. We believe that Congress should carefully study the impact of changes before imposing those standards on the fifty states, who represent a consensus on the appropriate prohibitions against deceptive practices.

Question 3. What would be the costs, if any, to the states of adoption of these proposed federal changes?

Answer. The financial costs are, first, the preparation litigation in all fifty states of cases to resolve the effect of the federal changes on the state standards. These matters will take several years of trial and appellate litigation to resolve.

Second, the costs of expert economic testimony. These costs would make states' enforcement efforts much more costly, and considerably slower. The net result is reduced efficiency. State's will have to bear these costs at once, until there is a definitive decision from the highest state courts on the effect of the changes. If the decision is that the FTC amendments are binding on that state, the additional costs will be permanent. The result is reduced efficiency, and considerably higher institutionalized costs. The states cannot afford these costs, and do not believe they generate useful testimony.

Third, there are costs to businesses and consumers by a looser definition of deceptive, which would allow greater latitude for deceptive practices, and make it more costly for such practices to be stopped. No economic impact analysis has shown that the changes are economically efficient, or of benefit to the states, to business, or to consumers.

Lastly, the states have built an interdependent system of law and enforcement of mutually agreed standards with the federal government. The first cost is to the principle of federalism, where the states cooperatively have worked together and with the federal government to stop deceptive practices. A unilateral change by the federal government will disrupt a unique example of effective federal-state cooperation.

Question 4. Would a statement of Congressional intent to the effect that any federal changes should not be construed to affect state law be sufficient to solve the states' problems with these proposals?

Answer. A statement of intent, while an effort to avoid a unilateral federal amendment of the state statutes, would address few of the states' concerns. While the state attorneys general feel such a statement of intent is better than Congress' simply ignoring their concerns, such a statement would merely assist the cause in the inevitable relitigation of the underlying issue: the effect of FTC precedent.

As practicing attorneys in offices going into state court daily, we can assure you that such a statement hardly guarantees that the result. The question will only be resolved through litigation over the coming years. The chances are that some state court will limit the effect of federal amendments, and other state courts will not, and will result in a de facto amendment of the state law in those states.

Secondly, the costs of relitigating the issues is one the states do not think is an economy. It is economically and governmentally inefficient to relitigate settled issues, when the states feel the present statutory scheme is working properly.

Third, the states will have to pay for the expert testimony that the amendments require until the issue is resolved. For those states where the Federal amendments are found binding, the significant unwanted costs and delay of such testimony will be an added governmental burden in a time of great need for economy and efficiency.

Fourth, the states are not effectively able to enforce higher standards than the federal government. Any state attorney general who has undertaken the litigation necessary to regulate a national advertising campaign will tell you that states cannot effectively enforce their laws on interstate advertising by respected companies, even if the advertising offends state law. The FTC sets the national ethic on deception.

QUESTIONS OF THE MINORITY AND THE ANSWERS THERETO

Question 1. If the statutory change in the FTC's deception autority expressly disclaimed any intent to effect little FTC acts, would this alleviate the problems outlined in your testimony?

Answer. I believe this question is essentially the same as the questions addressed in the four questions addressed by the majority. In essence, the matter will only be resolved by the state courts, many under specific state statutes requiring them to follow federal precedent. A federal disclaimer will only give the states assistance in arguing against such effect. The legal effect remains in doubt. As set forth in my answer to question No. 2 to the majority, the practical effect is even more doubtful. The states do not have the resources or the tools to regulate national deceptive practices. If practices that are currently held to be deceptive are permitted by the federal government on a national scale—in fifty states, the states will have a sorry time trying to apply stricter standards to local practices. The federal standards inevitably become the local standards.

Question 2. Should the Commission protect the foolish, gullible and ignorant consumer?

Answer. Yes. The question could be rephrased to be, whether the Commission should protect the most vulnerable members of our society, the ones most likely to be preyed upon by unscrupulous business. If anyone deserves protection, it is certainly these people. Such consumer frauds are tried and true. For instance, we have recently filed a motion for contempt in Vermont against a business which mailed out postcards telling consumers that they had won a prize, to be picked up at a local motel. An unemployed Vermonter received one, and responded. When he arrived, he received a lengthy sales presentation on how he was taking insufficient care, as a father, of seeing that his children were properly photographed during their childhood. When he appeared ready to sign up for $500 in photographic services, he was told that his prize was $20 in cash, which he could apply to his downpayment. He signed. When he could not afford the payments, and requested a reduction in the monthly payment, he was rudely told that he had a legal obligation. The phony contest was obviously deceptive, sadly preying on ignorant, gullible, or foolish consumers. Consumers victimized by the worst business practices should not receive the most modest protection. It makes no sense to place additional barriers of proof to deceptive practices—such as requiring proof of common law fraud—in the most egregious situation. Such a requirement will only make such practices more prevalent, and hobble the FTC and the states in addressing them.

Question 3. Chairman Miller believes the duty of the FTC is to consumers not to competitors, would you agree?

Answer. I do not. A deceptive pricing policy, for instance, by a business affects not only consumers, but competitors. If a business can increase its sales through deceptive pricing, usually it takes those sales directly from more ethical competitors, profitting from the illegal practice. The competitor is then in the position of reducing his ethics to the deceptive level, or of losing his sales volume. Consumer fraud regulation protects honest businessmen as well as consumers, by upholding the standards of the marketplace to insure the dissemination of accurate product information, resulting in greater market efficiency, more informed consumers, and fairness to ethical business practices. Many attorneys general, my office included, work closely with business in stopping deceptive trade practices which hurt both the consumer and the reputable business competitor.

Senator **Kasten**. Next will be a panel with Mr. Rein, Mr. Silbergeld, Mr. Myers, Mr. Daniel, and Mr. Versfelt.

Our first witness of this panel is Mr. Bert Rein, representing the U.S. Chamber of Commerce.

Mr. Rein.

STATEMENTS OF BERT W. REIN, ON BEHALF OF U.S. CHAMBER OF COMMERCE; MARK SILBERGELD, DIRECTOR, WASHINGTON OFFICE, CONSUMERS UNION; MATTHEW L. MYERS, ON BEHALF OF THE COALITION ON SMOKING OR HEALTH; PAUL DANIEL, ON BEHALF OF BROWN AND WILLIAMSON TOBACCO CO.; AND DAVID S. VERSFELT, ON BEHALF OF THE AMERICAN ASSOCIATION OF ADVERTISING AGENCIES, INC., ACCOMPANIED BY GILBERT H. WEIL, ON BEHALF OF THE ASSOCIATION OF NATIONAL ADVERTISERS, INC., AND WILLIAM W. ROGAL, ON BEHALF OF THE AMERICAN ADVERTISING FEDERATION

Mr. **Rein**. Thank you, Mr. Chairman.

My name is Bert Rein, and I am appearing on behalf of the Chamber of Commerce of the United States.

The chamber welcomes this opportunity to explain its advocacy of defining "deception" under Section 5 of the FTC Act. We believe the extensive record being made on the issue of deception should serve as a key step in formulating the legislative guidance we believe to be essential.

The chamber's deception position is one part of its overall approach to FTC reform which was presented to the committee in March. The chamber seeks neither to praise the FTC nor to bury it. Instead, we are asking the Congress to define and harmonize the well springs of FTC power under section 5. That is, unfair acts or practices, deceptive acts or practices, and unfair methods of competition.

We seek to give the Commission a reasonably bounded mandate to guide its actions and to facilitate meaningful review by the courts and the Congress. We recognize that, even in the absence of a defined mandate, the Commission may reach good results as well as bad ones in specific cases, and we know that the Commission is always subject to the pressure of congressional oversight. We believe, however, that a delegation of essentially arbitrary power in matters affecting speech is totally inconsistent with our constitutional system and cannot be defended by any alleged need to preserve flexibility or to preserve scarce enforcement resources by permitting arbitrary action.

It has always surprised us that those who most ardently resist any restriction on the scope of sweeping FTC deception or unfairness powers would be in the forefront of opposition to other comparable limitations on individual liberties, particularly those administered with a liberal dose of administrative discretion.

In our written testimony we commented at length on the capacity or tendency to deceive test which seems to be the sole settled fruit of 44 years of FTC litigation. We have pointed out that this "I know it when I see it" circumlocution is implemented through application of the Commission's own expertise in discerning the express and implied messages of acts and practices, and that the Commissioners must cast themselves in the role of the ignorant, the unthinking and the credulous to apply this expertise.

We have shown that this capacity or tendency test requires no proof of harm to consumers or even materiality of the allegedly deceptive representation. We have established that Commission action is often taken without regard to the possibility of suppressing information like comparative pricing which is of enormous value to the vast majority of consumers.

Perhaps most importantly, we have demonstrated that deception has been used to attack a multitude of alleged sins by the FTC ranging from blatant flimflam to all children's advertising to safety defects in 40-year-old farm equipment to the absence of care labeling on carpets and to the omission of octane postings on gas pumps.

Our review of FTC deception persuades us that it has lost its character as a remedial tool against harmful market abuses and become a regulatory tool which enables the Commission to intervene whenever the flow of market information needs perfecting in the Commission's own expert judgment. We find little disagreement in the record over this potential for abuse. Instead, the debate focuses on whether reform proposals would excessively curtail legitimate remedial jurisdiction.

The chamber's proposals are designed to recognize two useful threads in FTC precedent. First, the FTC can usefully crack down on those who knowingly or recklessly convey false or misleading information by statement or act. This focus on seller conduct is essential to perserve an honest marketplace and the credibility of all advertising. It is the sound basis for the doctrine of substantiation which requires an advertiser to have an appropriate basis for affirmative claims before they are made. The chamber's proposal is thus intended to place a clear, direct congressional imprimatur on reasonable substantiation.

Second, where an alleged misrepresentation is unintentional, the chamber believes that the FTC can usefully intervene where reasonable consumers could rely on false or incomplete information to their detriment and where the benefits of suppressing the deceptive practice outweighs the benefits of giving advertisers latitude in areas of public debate which may be of substantial value to consumers.

In choosing language to pursue this objective, the chamber intentionally selected the same words the Commission itself used in its statement on unfairness and the words this committee has written into S. 2499 with respect to unfairness.

If an act which is unfair to consumers should be subject to this kind of analysis before it justifies Commission remedial action, there is no reason to avoid the selfsame inquiry when a representation is alleged to be unintentionally false or misleading. It seems difficult to understand why that inquiry is done easily and with reasonable degrees of evidence in the context of unfairness proceedings, but appears to turn impossible when the word changes from "unfairness" to "deception".

As our written testimony emphasizes, the Chamber is not irrevocably wedded to any specific language. We are committed, however, to obtaining legislative action in a reasonable time to insure that the FTC's deception mandate is made meaningful and useful.

We would point out to this committee that if that task is accomplished it should be as valid on the State level as it is on the Federal level. We see no reason why the Congress' consideration of this problem should be frozen by the fact that State legislatures have chosen at this time to take their guidance from the Congress. If Congress modifies its guidance, State legislatures should choose either to continue to follow the congressional mandate or, if they so desire, to strike out on their own.

Thank you, Mr. Chairman.

[The statement follows:]

STATEMENT OF BERT W. REIN ON BEHALF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES

Mr. Chairman and members of the Committee, my name is Bert W. Rein. I am the principal of a professional corporation that is a member of the law firm of Kirkland & Ellis here in Washington, D.C. I am a member of the U.S. Chamber's Council on Antitrust Policy and have worked with its Federal Trade Commission Subcommittee in the development of the Chamber's position on legislative issues affecting the Commission. Accompanying me today is Fred Byset, the Chamber's Associate Director of Government and Regulatory Affairs for Antitrust.

The Chamber participated actively in this Committee's hearings earlier this year concerning the proper role of the Federal Trade Commission in our competitive economy. We welcome this opportunity to supplement our previous statement and present the Chamber's views on the need to define the FTC's "deception" authority.

Recent Congressional consideration of proposals to reform the Federal Trade Commission Act has confirmed a growing concern among scholars and practitioners that the Act's vague mandate to remedy "unfair or deceptive" acts and practices fails to provide meaningful enforcement guidance to the Commission, the courts and the business community.[1] Lacking meaningful legislative direction, the Commission appears to oscillate between extremes and is criticized both for inactivity and for broad, activist, regulatory intervention in the market. As Senator Danforth observed during the 1979 FTC oversight hearings, "unfair and deceptive acts or practices, that is just whatever the FTC says it is, "a nonstandard where "the sky's the limit.[2]

In S. 2499,[3] this Committee endorsed a new subsection to Section 5 of the FTC Act providing enforcement guidance for the Commission's "unfairness" authority. The Committee Report also noted that the Committee found "merit" in various criticisms that had been raised concerning the FTC's "deception" powers, including the following four points:

First, in interpreting the meaning of a particular ad, the Commission has relied on its own expertise, often without direct evidence of how consumers would understand the ad. Second, the Commission's interpretation of advertising has not always been based on what consumers acting reasonably in the circumstances would understand the ad to mean. Third, the Commission has sometimes acted without evidence that the challenged ad was likely to injure consumers. Finally, the Commission's decisions may have sometimes harmed consumers, rather than protecting them, because they have suppressed truthful and useful information. Id. at 4.

Recognizing the difficulty and sensitivity of finding legislative language which would remedy these problems without restricting or appearing to restrict the FTC's ability to challenge unethical market practices, the Committee scheduled the present hearings to explore the "deception" issue in further detail.

In reforming the FTC's "unfairness" authority, the Congress is addressing a concept which exists only in the eye of the beholder and one which has had limited independent use in FTC case law.[4] The concept of "deception", however, has apparent roots in the common law and the ordinary language advantage or connoting devious and unethical behavior. Thus, efforts to reform the FTC's deception authority raise sensitive questions because they may be made to appear to give latitude to the miscreant. This sensitivity is compounded by a substantial body of FTC case law on deception which is used to argue that deception law is "well settled" and reasonably bounded.

At the same time, the Chamber believes that an examination of the FTC's historic exercise of deception authority fully supports recent criticisms levelled by Chairman Miller and legal commentators, as well as the Committee Report on S. 2499. There is today little similarity between the common law doctrine of deception, from which FTC practice draws its nomenclature, and the FTC's independent legal approach; FTC case law and judicial precedent simply do not provide predictable boundaries for FTC deception jurisdiction. Rather, the FTC has merged unfairness and deception into a single, amorphous concept under which the FTC can both check market abuses *and* act affirmatively to "perfect" the flow of information under its own model of a properly functioning market. Although originally intended as a remedial

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[1] E.g., R. Posner, Regulation of Advertising by the FTC (Am. Enter. Inst. for Pub. Policy Research, Nov. 1973); Report of the ABA Commission to Study the Federal Trade Commission 92 (Sept. 15, 1969) (separate statement of Richard A. Posner); Beales, Craswell, & Salop, The Efficient Regulation of Consumer Information, 24 J.L. & Econ. 491 (1981); Gellhorn, Proof of Consumer Deception Before the Federal Trade Commission, 17 Kan. L. Rev. 559 (1969); Grady, "Regulating Information: Advertising Overview," in The Federal Trade Commission Since 1970: Economic Regulation and Bureaucratic Behavior, at 222 (K. Clarkson & T. Muris eds. 1981); Millstein, The Federal Trade Commission and False Advertising, 64 Colum. L. Rev. 439 (9164).

[2] Oversight of the Federal Trade Commission: Hearings Before the Subcomm. for Consumers of the Senate Comm. on Commerce, Science and Transportation, 96th Cong., 1st Sess. 35, 36 (1979). As Senator Danforth further remarked: "The problem comes, as I understand it, with unfair or deceptive practices. That is the open door through which all of the tanks and trucks and everything else pour through . . . . What can we do to tighten this up?" Id. at 36.

[3] S. Rept. No. 451, 97th Cong., 2d Sess. (1982).

[4] The FTC, consistent with the language of Section 5 and the history of the Wheeler-Lea Amendment which introduced the "unfair or deceptive" concept without clearly distinguishing unfairness and deception, has often issued complaints charging the same act as unfair or deceptive.

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tool to correct aberrant business conduct, the FTC's "deception" authority has not become a regulatory tool to impose shifting FTC policy preferences on the competitive economy.

The U.S. Chamber concurs in Senator Danforth's suggestion during the 1979 oversight hearings that the "responsible way" for Congress to approach this problem is to address the basic "definitional question" of the FTC's statutory "deception" powers.[5] To this end, the Chamber has proposed draft legislative language which, if adopted, would preserve the legitimate remedial core of the FTC's deceptive practices doctrine while counteracting the agency's more expansive regulatory interpretations and preserving reasonable First Amendment latitude for commercial speech.

I. THE TRADITIONAL CONCEPT OF DECEPTION AT COMMON LAW

The common law tort of deceit has developed, over centuries of judicial interpretation, a relatively well-defined content and rich body of precedent.[6] While the common law is often denigrated as caveat emptor ("buyer beware"), common law deceit has, in fact, evolved as a reasonable protection for buyers against dishonest or reckless conduct which causes them injury. At the same time, common law deceit limits judicial intervention to injury situations where there is misconduct on the seller's part to be remedied.

Thus, the modern common law action for deceit focuses first on the question whether the seller intentionally has departed from accepted commercial norms. A cause of action in deceit is stated if the seller misrepresents a material fact knowing that it is untrue or with reckless disregard for whether it is true or false.[7] Similarly, if a statement is susceptible to several interpretations, one of which is false, a seller will be held liable where he either intended to convey the untrue interpretation or else recklessly failed to consider how the statement might be misconstrued.[8]

Beyond assessing the quality of a seller's conduct in determining the need for remedial intervention, the common law limits intervention to situations where misconduct might "reasonably" be found to have an adverse effect. In the case of an allegedly ambiguous statement, for example, the jury considers whether they, as reasonable persons, would find the statement capable of double-meaning. In addition, the alleged misrepresentation must be sufficiently "material" so that a reasonable person would attach importance to the statement in determining his course of action. A plaintiff purchaser must still prove that he reasonably and jusitifiably relied on the statement to his detriment.[9]

In this latter connection, the common law doctrine of deception requires proof of actual injury or harm resulting from the misrepresentation as a prerequisite for judicial action. For example, where a plaintiff relies on a misstatement to purchase a product that is of equal value to the product as represented, nominal damages are not available.[10] Thus, the judicial process at common law intervenes in the market only to remedy specific economic harm.

Because the essential elements of common law deception are clearly defined, the honest seller enjoys reasonable latitude in promoting his products to the public. He cannot be challenged on misimpressions he did not intend to convey, for unforeseeable interpretations of ambiguous statements, or for insignificant injuries. On the other hand, the defrauded consumer who has acted reasonably is entitled to meaningful relief including punitive damages as a significant deterrent to further misconduct.

II. DECEPTION AT THE FTC

The Federal Trade Commission's consumer protection jurisdiction over acts and practices that are "unfair or deceptive" was added to Section 5 of the FTC Act by the Wheeler-Lea Amendment of 1938. Although relatively sparse, the legislative history of that statutory language suggests that Congress intended the FTC to apply a concept of "deception" similar to the well established common law doctrine in order to remedy actual harms resulting from misleading sales practices.[11] FTC jurisdiction, however, would enhance the enforcement of deception rules by permitting nationwide enforcement and removing the burden of litigating expense from injured consumers.

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[5] Oversight of the Federal Trade Commission: Hearings Before the Subcomm. for Consumers of the Senate Comm. on Commerce, Science, and Transportation, 96th Cong., 1st Sess. 37 (1979).

[6] For a discussion of the common law roots of deception, see T. Plucknett, A Concise History of the Common Law 640–43 (5th ed. 1956); W. Prosser, Handbook of the Law of Torts 685–86 (4th ed. 1971).

[7] See Restatement (Second) of Torts § 526 & comment e (1977).

[8] See id. § 527.

[9] See id. §§ 537, 538.

[10] See W. Prosser, Handbook of the Law of Torts 731, 734 (4th ed. 1971).

From this rather straightforward beginning, the FTC expanded and developed its "deception" authority far beyond traditional common law principles. Rather than pursuing and redressing specific consumer harms, the Commission has laid claim to broad and plenary power to regulate the content and flow of commercial information. Because the Commission's version of "deception" has become a jurisdiction without boundaries, Congress is faced with a situation where both sound economic policy and First Amendment values counsel legislative direction of FTC enforcement priorities.

The four specific problems identified in the Senate Commerce Committee's report on S. 2499 provide an appropriate framework for analyzing the breadth of FTC deception authority. Whether considered individually or in their overall impact, these "problems" result from overly expansive Commission interpretations that can and should be addressed by the Congress through a more explicit statutory definition.

A. The FTC's Claimed Expertise To Interpret the "Meaning" of Seller Representations—Acts or practices can be deceptive—i.e. false or misleading—only if the representations they make to consumers are inaccurate in fact or so incomplete as to convey false impressions. For example, an advertisement which holds out a product at $5 may be misleading if the price is $6 or if the $5 price is available only with the purchase of another product. Whether the inaccuracy arises from direct misrepresentation or omission, however, its foundation is a comparison of the message conveyed to consumers with the true facts. Thus, in any deception controversy the message which a seller's acts or practices are deemed to convey is critical to the outcome.

For FTC purposes, neither the meaning a seller intended to convey (or recklessly conveyed), nor the reasonable interpretation of the seller's conduct, limits the scope of representations which provide a base for deception analysis. Instead a seller is held responsible for any representation which the Commission, using only its own expertise, finds the seller's conduct to make. No evidence is required that any consumer actually has believed the alleged misrepresentation or that any appreciable segment of the population would even recognize the subjective meaning that a majority of Commissioners perceive.[12]

Given virtually discretionary power to find both the express and implied messages in a seller's representations, the FTC is capable of regulating almost any commercial speech it finds distasteful. Once a majority of the Commission discerns a representation having the "capacity to deceive," the Commission has a basis for relief irrespective of the good faith intentions of the seller or the fact that no reasonable consumer would be misled. Moreover, this FTC power is insulated from review in the courts because perceived meaning, unlike accuracy, cannot be assessed for consistency with the record. As former Commissioner Pitofsky has observed, the broad discreation accorded the Commission in interpreting the meaning of an advertisement or other representation is the "principal reason that the Commission has managed to prevail in the appellate courts in the overwhelming majority of its [deception] decisions that have been appealed." [13]

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[11] Thus, the Senate report explained that the Commission should have jurisdiction to restrain unfair or deceptive practices which "deceive and defraud" the general public, and that the legislation would permit the Commission to stop the "exploitation or deception" of the general public. S. Rep. No. 221, 75th Cong., 1st Sess. 2, 3 (1937). During congressional hearings on the Wheeler-Lea amendment, legislators and the FTC's Chairman answered questions respecting the meaning of "deception" by indicating that the term was commonly understood. See Federal Trade Commission Act Amendments: Hearing on S. 3744 Before the House Comm. on Interstate and Foreign Commerce, 74th Cong., 2d Sess. 36 (1936) (statement of Rep. Lea questioning whether there could be any particular doubt about the meaning of "deceptive"); To Amend the Federal Trade Commission Act: Hearing on H.R. 3143 Before the House Comm. on Interstate and Foreign Commerce, 75th Cong., 1st Sess. 41 (1937) (statement of Rep. Crosser that "I do not think anybody has any difficulty" with the word "deceptive"); id. 12 (statement of FTC Comm'r Davis that "it does not seem to me that it takes an expert or a lawyer to know what deceptive means"); id. 59 (statement any citizen understands"). At the time of these hearings, of course, the common law concept of deceptive would have been the commonly understood standard.

[12] The Commission's ability and willingness to reply on its own expertise in defining the message conveyed by a seller is well recognized. See 15 J. Von Kalinowski, Antitrust Laws and Trade Regulation, § 122.03[1] (1981).

[13] Pitofsky, Beyond Nader: Consumer Protection and the Regulation of Advertising, 90 Harv. L. Rev. 661, 677–78 (1977).

The *Dannon Milk Products, Inc.* case [14] illustrates the Commission's virtually unlimited power to attack almost any advertisement by manipulating its message. There, the Commission held, solely on the basis of its own intuition and subjective reactions, that "many consumers" would be likely to interpret the declaration that yogurt is "nature's perfect food" to mean that yogurt supplies "all of the nutrients essential for maintenance of life, growth, development and so on" (id. at 856). Since yogurt does not contain every essential nutrient known to man, the Commission's subjective interpretation of the claim effectively guaranteed an ultimate finding of deception.

Similarly, in *General Motors Corp.*, the Commission charged that General Motors had engaged in deceptive acts and practices when it advertised that Road and Track magazine found the Vega to be the best handling passenger car ever built in the U.S. There could be no dispute that the primary message was truthful and accurate because Road and Track had in fact published the remarks attributed to it. Nonetheless, the Commission intuitively inferred a much broader meaning, i.e., a claim by General Motors that it had data which showed that Vega really was the best handling car. Because General Motors had not run expensive comparative handling tests to substantiate that broader claim—a claim that General Motors never intended nor reasonably anticipated—a finding of "deception" became inevitable.[15]

Even when the Commission considers evidence beyond its own subjective perceptions, it sometimes finds corroboration for its intuitive conclusions in the scarcest of records. In the *Gelb* case,[16] for example, the Commission interpreted an advertisement for "permanent" hair coloring to represent that no treatment of after-grown hair would be required, resting on a single consumer who testified—after much prodding—that some other consumers might interpret the claim in that way though she herself knew better. In another instance, the FTC staff charged that the Firestone Tire Company's trade name "Safety Champion" represented that the tire was safer than any other brand, despite a scientific survey establishing that only 1.4 percent of the surveyed consumers so interpreted the name.[17]

As these examples confirm, this Committee has correctly identified a fundamental flaw in the "deception" doctrine as currently applied by the FTC. If the legal meaning of an advertisement or other representation is simply what three out of five Commissioners say it means, irrespective of the seller's intent or evidence of reasonable consumer reaction, sellers can never be confident that their conduct will survive FTC scrutiny. Particularly since the Commission considers it "deceptive" for an advertiser not to test product claims prior to making them, the essentially unlimited power of the Commission to interpret what a claim means may create impossible "Catch-22" situations where an advertiser is guilty because he has not previously substantiated a claim he did not, or could not, know he was making.

Permitting the FTC to pursue enforcement based on its own reactions to seller representations, rather than consumer reactions, creates a substantial risk of enforcement priorities reflecting Commission social judgments rather than consumer needs. All too often, the Commission expends the bulk of its resources on curing alleged information deficiencies—which it believes lead consumers to value a product too highly or compare it inadequately with competing products—by finding sellers, absent affirmative disclosures, to advance exaggerated (and hence misleading) product claims.[18] The Commission is thus able to place the moral force of a deception finding behind an affirmative regulatory effort to direct the flow of commercial speech.

B. The absence of a "reasonable consumer" standard.—Whether the meaning of a seller's representations is discerned by FTC intuition or determined by evidence, the message received will not be the same for all consumers. Any statement, however clear or accurate, can be misread by a few careless persons or misconstrued by a few hyperimaginative ones. Thus, the degree of care or intelligence attributed to the consumer whose "deception" is considered actionable is critical to the scope of FTC enforcement power. Under the common law, which applies a consistent standard of reasonableness, the fact that careless or thoughtless consumers may be misled by messages which convey valuable, accurate information to reasonable consumers does not justify intervention unless the seller intended to harm the vulnerable targets. By contrast, the Commission's deception precedent fails to articulate a clear or uniform standard for the deceived consumer and the FTC has, in practice, taken action where only a consumer exercising minimal diligence or mental capacity could be misled.

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[14] 61 F.T.C. 840 (1962).

[15] 85 F.T.C. 27 (1975) (consent decree).

[16] 33 F.T.C. 1450 (1941), aff'd, 144 F.2d 580 (2d Cir. 1944).

[17] Based on these allegations, an FTC Administrative Law Judge issued an Order precluding further use of the "Safety Champion" name, although the FTC itself ultimately reversed on this point. Firestone Tire & Rubber Co., 81 F.T.C. 398 (1972), aff'd, 481 F.2d 246 (6th Cir. 1973).

[18] A seller may be found to be making claims either through advertising, or other affirmative action, or simply by continuing to allow his product to circulate in commerce without correcting the alleged information deficiency. See International Harvester Co. 3 Trade Reg. Rep. (CCH) ¶ 21,820 (April 29, 1981) (order denying motions to dismiss). See also infra Section III.

Some Commission decisions have suggested that the relevant interpretration is that which the "average" individual or the "general public" would give a claim. There is, however, substantial authority for the proposition that the Commission buy bring a charge of deception on the basis of a representation's impact on "the ignorant, the unthinking and the credulous," [19] that the Commission may interpret an adverstisement as a careless reader would,[20] and that the Commission may insist that statements be so unambiguous that " 'wayfaring men, though fools, shall not err therein.' " [21] Thus, over the years, the Commission had found that the trade name "First Prize" bobby pins might cause a consumer to think that the product had received an award for quality or design,[22] has found that consumers might interpret a skin-moisturizing product with the trade-name "Rejuvenescence Cream" to imply that the product would restore the appearance of youth to skin regardless of the condition of the skin or the age of the user,[23] and has found that consumers might interpret advertising of a "permanent" hair-coloring product as promising that the product would color even hair that had not yet grown.[24]

More recently, the Commission upheld summary judgment that a Ford Motor Company advertisement had deceptively implied that the consumer would actually get the advertised fuel mileage in normal long-distance driving, despite the advertisement's explicit qualifications that mileage varies according to maintenance, equipment, total weight, driving habits, and road conditions, that no two drivers or cars are exactly the same, and that the consumer might actually average less or more than the advertised fuel efficiency.[25] Given the clear disclaimers in the ad, the Commission's finding of a deceptive implied "meaning," solely on the basis on its own expertise and without considering a survey conducted by Ford, necessarily premised enforcement upon the assumed perceptions of those consumers who were either unable or unwilling to read the entire ad. The FTC thus suppressed information of substantial value to reasonable consumers.

The failure of the FTC to articulate and apply a consistent standard based on the common law concept of the "reasonable" consumer has also impaired judicial review of Commission decisions involving deception issues. Without a uniform objective consumer standard, the courts have little basis upon which to assess the Commission's message interpretations. This, in turn, reinforces the tendency of the courts to defer broadly to the assumed "expertise" of the FTC in deception matters and to accept unqestioningly the agency's subjective interpretations of the "meaning" of seller representations. Particularly since neither the FTC's members nor the Federal Judiciary are especially good surrogates for the "ignorant, the unthinking and the credulous," the use of that standard effectively means that sellers will be held to whatever representation the Commission finds useful in forging relief.

Once again, it appears that the concern raised in the Committee Report is well founded. As a practical matter, the FTC has developed a unique concept of deception which permits an advertiser providing valuable information to reasonable consumers to be held in violation of federal law because hpopthetical ignorant, unthinking or credulous consumers may themselves distort his message.

C. The importance of proven detriment to consumers.—Not all false or misleading representations by sellers cause injury to consumers. As recognized through common law experience, certain information is simply not relevant to a consumer's buying decisions. For example, an advertisement may not accurately capture the standard white color of a particular appliance—and thus misrepresent the product—but this error may have no discernible impact on sales. Similarly, consumers relying on a misleading statement need not be harmed. For example, a display may lead consumers to believe that a product costs $5 when it is actually on sale for $4 and thus mislead buyers as to price without injuring them when they receive a $1- reduction.

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[19] *Aronberg* v. *FTC,* 132 F.2d 165, 167 (7th Cir. 1942). Cf. *Exposition Press, Inc.* v. *FTC,* 295 F.2d 869, 872 (2d Cir. 1961) cert. denied, 370 U.S. 917 (1962) (interpreting an advertisement from the point of view of the least sophisticated reader).

[20] See *General Motors Corp.* v. *FTC,* 114 F.2d 33, 36 (2d Cir. 1940), cert. denied , 312 U.S. 682 (1941); *Independent Directory Corp.* v. *FTC,* 188 F.2d 468, 470 (2d Cir. 1951).

[21] *General Motors Corp.* v. *FTC,* 114 F.2d at 36.

[22] Reiser Co., Inc., 61 F.T.C. 1378 (1962) (deceision of hearing examiner).

[23] *Charles of the Ritz Distributors Corp.* v. *FTC,* 143 F2d 676 (2d Cir. 1944).

[24] *Gelb.* v. *FTC,* 144 F.2d 580 (2d Cir. 1944).

[25] Ford Motor Co., 87 F.T.C. 756 (1976).

The common law standard of "detrimental reliance" limits judicial intervention to situations where consumers actually make harmful decisions based on false or misleading information. The "detrimental reliance" concept recognized that consumers make judgments based on the totality of market information, rather than isolated fragments, and thus permits competitor advertising and consumer reaction to play the major role in disciplining sellers. The "detrimental reliance" concept also acknowledges that government intervention in the information market always creates risks to the future flow of useful information, and the freedom of commercial speech. Such intervention is justified only where those risks are outweighed by the need to remedy actual consumer injury.

The FTC's deception precedents, departing from the common law, reject the need even to analyze consumer reliance or consumer injury from an alleged misstatement. Apparently influenced by the fact that an FTC challenge is brought by the agency staff—rather than by injured consumers—the Commission has rested entirely on the notion of "capacity" or "tendency" to deceive without considering the practical likelihood of consumer reliance or injury.

For example, in *Exposition Press* v. *FTC*, 295 F.2d 869 (2d Cir. 1961), cert. denied, 370 U.S. 917 (1962), the Commission upheld sanctions for deceptive advertising against a "vanity publisher" who had advertised that authors contracting with the publisher 40 percent royalties without disclosing that, as with all such publishers, the author would be required to finance the initial cost of publication. The advertisement, however, merely solicited the reader to send for a free brochure which clearly disclosed, as did all contracts signed with the company, that authors must underwrite publication costs. The Court of Appeals upheld the Commission's decision. Judge Henry Friendly dissented, noting the remote possibility that any budding author would believe that publication was both unscreened and free. Judge Friendly cogently observed that "any remote tendency of the ad to mislead was ended when the brochures arrived," and that the only prejudice suffered by the prospective author would be the cost of a stamp and "the depression when the brochures dissipated the temporary euphoria of thinking their books would be published without cost." 295 F.2d at 875.

Similarly, in *FTC* v. *Colgate-Palmolive Co.*, 380 U.S. 374 (1965), the Supreme Court specifically endorsed the Commission's view that actual detriment to the consumer is not a necessary element of a Section 5 deception case. In Colgate, an advertiser, attempting to demonstrate on television that its shaving cream would enable a razor to shave sandpaper, used a simulation because actual sandpaper would have been indistinguishable on television from ordinary colored paper. The Court held that failure to disclose that the demonstration was simulated was a "deceptive" practice, notwithstanding that the product would indeed shave sandpaper as claimed. Justice Harlan's vigorous dissent protested that "[i]f the image [the viewer] sees on the screen is an accurate reproduction of what he would see with the naked eyes were the experiment performed before him with sandpaper in his home or in the studio, there can hardly be a misrepresentation in any legally significant sense."[26]

A legal doctrine which permits the Commission to commit enforcement resources without regard to detrimental reliance inevitably leads to misplaced priorities. It substitutes the Commission's instinct for what is wrong for the market experience of consumers as a guide to where government intervention is warranted. In a society where commercial speech is constitutionally protected, it is difficult to see why the FTC ought to have power to interfere with the speech rights of sellers without demonstrating countervailing substantial injury to buyers.

The Commission, of course, may properly be concerned with the overall deterioration of market standards in situations where knowing falsehoods and intentionally misleading representations are involved. Even when the immediate harm is minor, fraudulent or reckless communication may impose enormous costs on sellers and consumers as a group. If consumers are exposed to constant flimflam, they will become skeptical about the truth of all advertising. Widespread skepticism would impair the ability of even the most scrupulous and careful seller to publicize the worth or superiority of its products and could compromise the legitimate function of advertising as a source of information useful to consumers.[27] There may thus be benefit in the Commission's pursuit of intentionally false or reckless representations without regard to immediate injury and irrespective of whether the product involved sells for fifty cents, five dollars, or five thousand dollars.

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[26] 380 U.S. at 396. The Commission has successfully challenged "deceptive" practices in numerous other cases in which the alleged misrepresentations did not detract from the quality of the product. See, e.g., Fuller Tool Co., 62 F.T.C. 1328 (1963) (failure to disclose that product was manufactured in foreign country); Frank A. Kerran, 54 F.T.C. 1035 (1958) aff'd, 265 F.2d 246 (10th Cir. 1959) (failure to disclose that oil was re-refined, irrespective of offer of proof that re-refined oil is of equal quality to virgin oil); *FTC* v. *Royal Milling Co.*, 288 U.S. 212 (1933) (respondent's name might imply that it ground grain itself, whereas it packaged grain ground by others); *Korber Hats, Inc.* v. *FTC*, 311 F.2d 358 (1st Cir. 1962) (that termed "Milan" must be manufactured of wheat straw, not hemp, although consumers might not perceive a difference). In none of these cases was there evidence that the alleged "deception" influenced or injured consumers.

On the other hand, where neither fraudulent actions nor substantial departures from market norms of reasonable care in communication are involved, there appears to be little benefit in expending Commission resources in the absence of adverse consumer impact. By definition, attacks on innocent misrepresentations have little deterrent value since the conduct is unintentional. Indeed, the principal effect of such attacks may be to raise the cost of advertising and create a climate of caution inconsistent with First Amendment rights. The absence of provable injury, or a substantial threat of injury, is a clear market signal that consumers can deal with the alleged problem without Government help. It is also an excellent indicator that market forces can impose a substantial incentive to maintain communications quality.[28]

D. Possible suppression of useful commercial information.—It is a truism that all information is incomplete and hence inherently less than completely accurate. Thus, were the FTC to apply its "capacity to deceive" standard literally, virtually all commercial speech could be enjoined or regulated through affirmative disclosure orders. Both resource constraints and an implicit recognition that the value of useful information must be weighed against its imperfection, have foreclosed the Commission from going to the extreme. Nevertheless, the Commission's deception precedent, as noted in the Commerce Committee Report, fails to provide guidance on how the social benefits of speech latitude are to be weighed against the costs of imperfect information.

On one level. notions of fairness and due process are offended when an honest seller is held strictly liable for an unintended—and perhaps even unreasonable—interpretation of his advertisement, based solely on the subjective reactions of a majority of individual Commissioners. In such instances, both the Commission's credibility and the public's respect for the FTC can be significantly diminished.

On occasion, Commission action under its ill-defined "deception" rubric has also been distinctly anti-consumer. When the Commission challenges advertising that has only a mere "tendency" to mislead a small minority of consumers who might read an ambiguous statement in an unintended way, it simultaneously deprives the majority of consumers who interpret the advertisement in its intended sense of correct and useful information.[29] As Commissioner Bailey's dissent in the recent *Kroger* case noted, the order at issue there would "chill the development of useful comparative price advertising, especially among retail grocers, which is extremely useful to the public, particularly in times of high inflation." [30]

Finally, in addition to being anti-consumer, the Commission's regulation of "deceptive" acts and practices has often been anticompetitive. Former Commission Pitofsky, for example, has noted that the FTC's fictitious pricing" cases have generally attacked discount houses, usually because a non-discounting seller has filed a complaint against a lower-priced competitor.[31] In a similar vein, Professor (now Judge) Posner, as a participant in the extensive ABA study of Commission's enforcement activity, observed that the FTC cases have often focused on "practices, not involving serious deception, by which sellers have attempted to market a new, often cheaper, substitute for an existing product." [32]

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[27] Moreover, a "Gresham's Law" phenomenon could develop with unrestrained advertising simply driving more careful representations out of the market.

[28] Where commercial success depends upon repeat sales, the marketplace will effectively deter claims that disappoint consumer expectations. While the questionable claim may induce a consumer to purchase the product once, the dissatisfied user will not become the repeat customer upon whom long-run profitability depends. In such cases, where the market can quickly and efficiently respond to seller exaggeration, lengthy and expensive regulatory proceedings are unjustified and inappropriate as a matter of enforcement priority.

[29] Developments in the Law—Deceptive Advertising, 80 Harv. L. Rev. 1005, 1042-43 (1967).

[30] The Kroger Co., FTC Docket No. 9102 (Sept. 25, 1981) (dissenting statement of Commissioner Bailey).

[31] Pitofsky, Beyond Nader: Consumer Protection and the Regulation of Advertising, 90 Harv. L. Rev. 661, 688 (1977).

[32] Report of the ABA Commission to Study the Federal Trade Commission 109 (Sept. 15, 1969) (separate statement of Richard A. Posner).

E. The outer boundaries of FTC deception.—As analysis of the four specific deficiencies noted in the Commission Report demonstrates, the Commission has assumed broad regulatory power under its "deceptive" acts and practices jurisdiction by breaking the link between FTC deception and deception's common law, common sense meaning. For this reason, any claim that FTC deception is clearly defined and well understood is, in the Chamber's view, itself misleading.

In fact, the boundaries of the Commission's "deception" authority appear to be constantly shifting and becoming increasingly vague. Recent FTC decisions reflect yet a further expansion of the "deception" doctrine so that it is today virtually indistinguishable from the Commission's much criticized and equally unbounded "unfairness" authority.[33] There is thus a significant danger that current legislative efforts to reform the FTC's "unfairness" jurisdiction could well be nullified should the Commission simply shift the basis for intrusive regulatory proceedings from "unfairness" to "deception."

In the controversial children's advertising proceeding, for example, the Commission simultaneously invoked both prongs of its Section 5 consumer protection jurisdiction, claiming that "televised advertising directed to children too young to understand the selling purpose of, or otherwise comprehend or evaluate, commercials is inherently unfair and deceptive." [34] Because parents, rather than small children, actually purchase the products being advertised, however, there could be no "deception" in the traditional sense of the purchaser being misled. Rather, the Commission was attempting to assert that "deception" could cover any alleged imperfection in the information flow.

Another example of the Commission's interchangeable use of "deception" and "unfairness" concepts is the recent *International Harvester* case.[35] An Administrative Law Judge indicated that a manufacturer's failure to undertake a campaign to inform the public of certain product defects could be "deceptive" as well as "unfair" even though the manufacturer did not know of the defect at the time it sold some of the products and made no specific, relevant product claims. Unlike traditional concepts of deceptioin which relate to the advertisement and actual sale of a product, the *International Harvester* decision indicates that a "deception" may occur when a manufacturer fails to undertake affirmative actions to disseminate information acquired long after the sales transaction is completed.[36] Such an expansive definition of "deception" would empower the Commission to undertake, under the "deceptive practices" language, continued detailed regulation of product quality by threatening to force continuing adverse disclosures unless the product was modified to Commission taste.

This attempt to sever the traditional link between "deception" and actual selling practices is also reflected in FTC proceedings against advertising that depicts allegedly unsafe activities unrelated to the qualities of the advertised product. In recent years, for example, the Commission has challenged a cereal advertisement showing someone eating wild plants and an advertisement for rice depicting children using a stove without adult supervision.[37] Although such cases do involve commercial advertising, the advertisement's message is wholly truthful and the so-called "deception" is immaterial to the consumer's purchasing decision.[38]

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[33] The plain meaning of "unfair" appears to comprehend all "deceptive" acts or practices. On the other hand, it appears logical for "deceptive" activity to be a subset of unfair rather than a coextensive term. Unfortunately, the Commission has never attempted to draw the boundary of the subset.

[34] FTC Staff Report On Television Advertising To Children 11 (Feb. 1978) (emphasis added).

[35] 3 Trade Reg. Rep. (CCH) ¶ 21,820 (Apr. 29, 1981) (order denying motions to dismiss).

[36] The complaint in *International Harvester* alleged that the respondent had manufactured certain modes of gasoline-powered tractors from 1939 through 1975, that beginning in 1955 the respondent knew or should have known that the fuel tanks of these tractors would shoot forth a geyser of fuel if the gasoline caps were dislodged while the tractors were hot or running, and that the respondent failed to disclose adequately the facts concerning his safety hazard. In denying motions to dismiss this complaint, the Administrative Law Judge did not allude to the manufacturer's sales after it allegedly had become aware of the defects. Instead, the opinion specifically referred to hazards "unknow at the time of sale, but subsequently discovered," stated that "where a company subsequently becomes aware of potential hazards relating to the ordinary use of its product, it may be deceptive to fail to warn consumers and potential purchasers," and found a duty to disclose defects "whenever they become known whether or not any specific product claims have been made." Id. at 22,053, 22,054.

[37] General Foods Corp., 86 F.T.C. 831 (1975) (consent decree); Uncle Ben's Inc., 89 F.T.C. 131 (1977). The General Foods complaint explicitly charged that the advertisement was unfair and deceptive.

[38] While such cases might appropriately be brought on a theory of "unfairness," within whatever bounds Congress chooses to give that doctrine, stretching the concept of "deception" to

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The Commission has also used the "deceptive practices" language as a tool for forcing sellers to provide additional information simply because the Commission believes it might be helpful to consumers. Thus, in its original rulemaking concerning the posting of gasoline octane ratings, the Commission explicitly relied on a theory of "deception," in addition to unfairness grounds, not because anyone was misled, but because consumers might find additional information about octane useful.[39] Such judgments plainly have nothing to do with traditional concepts of "deception" and are, in any event, best left to the free play of market forces, rather than the changing preferences of FTC Commissioners.

In summary, given the elastic and evolving nature of "deception" enforcement under existing FTC precedent and its effective merger with the open-ended "unfairness" doctrine, the current statutory language is simply too vague to provide effective Congressional guidance to the Commission, the Courts, or the business community. Particularly if the Congress places enforcement limitations on the FTC's "unfairness" authority, the boundaries of deception may become more elastic. Thus, it appears reasonable for a Congress interested in setting enforcement boundaries and priorities to address both branches—i.e., "unfair" and "deceptive"—of the authority granted the FTC by the 1938 Wheeler-Lea Amendment.

IV. PROPOSED LEGISLATIVE CLARIFICATION OF THE FTC'S DECEPTION AUTHORITY

The task of drafting legislative language which would remedy the problems accurately perceived in the Committee Report is a delicate one. Congress cannot realistically draft a code of deception or attempt to re-resolve closed cases. Moreover, Congress should not signal any abatement of federal concern over fraudulent practices and departures from the ethical standards which make the marketplace function. At the same time, Congress can and should set enforcement priorities, provide meaningful guidance on the scope of legitimate federal concerns, and establish clear boundaries within which the Commission and courts can function.

In approaching the similar problem of reforming "unfairness," S. 2449 uses the tests of consumer injury, reasonable avoidability of injury, and cost-benefit assessment. These statutory provisions, suggsted by the FTC itself, do not define unfairness. They do, however, provide an analytical framework for decisions on FTC resource commitment and boundaries for government intervention in the market as well as a standard for review by courts and Congressional oversight committees.

Suggestions for a similar approach to FTC "deception" have been advanced earlier by the Chamber, Chairman Miller, the National Association of Manufacturers and the three major advertising association. While the language used by each of these groups varies in detail, the recommendations coalesce around two fundamental ideas: (1) the distinction between per se actionable knowing or reckless misrepresentations and unintentional misrepresentations; and (2) the need to bound enforcement efforts against unintentional misrepresentations by analysis of actual injury to reasonable consumers.

The Chambers's proposal, originally advanced on April 1, 1982 in hearings before the House Subcommittee on Commerce, Transportation and Tourism, provides parallel definitions of the FTC's "unfairness" and "deception" authority by declaring unlawful such acts and practices which:

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cover such practices is inappropriate. Carried to its logical conclusion, all beer commercials which include a car or other motor vehicle would be "deceptive" as encouraging drunk driving and the current motorcycle and in which the rider steps out of a bar and rides off into the night would have to be banned.

[39] 36 Fed. Reg. 23871, 23872-75 (Dec. 16, 1971). The Commision rescinded this original rule, mooting extensive litigation over its validity, when Congress enacted Title II of the Petroleum Marketing Practices Act, 15 U.S.C. §§ 2821-2824 (Supp. IV 1980). 43 Fed. Reg. 43022 (Sept. 22, 1978). The latter legislation, which explicitly authorized the Commission to promulgate an octane-posting rule, is the statutory basis for the current octane-posting regulations. See 44 Fed. Reg. 19160 (Mar. 30, 1979). Ironically, the Commission's octane-posting rule may itself mislead consumers into believing that octane in itself affects an automobile engine's power or general performance, whereas in reality octane relates only to a gasoline's capacity to reduce engine "knock."

Another example of the Commission's attempt to prescribe in detail the format and content of advertising under expansive notions of "deception" as well as "unfairness" is the "proposed rule concerning "Advertising for Over-the-Counter Drugs," announced Nov. 11, 1975 (40 Fed. Reg. 52631). Under this proposal, all advertising for OTC drug products would have been limited strictly to labeling language approved by the FDA, thus turning television commercials for such products into a dry recitation of ingredients, warnings, etc. The Commission properly terminated this unwise effort, after several years of costly proceedings, on May 1, 1981 (46 Fed. Reg. 24584).

(a) consist of material representations known to be false or made in reckless disregard of their truth or falsity, or (b) directly cause or may foreseeably result in substantial economic injury to consumers and such injury is neither reasonably avoidable by consumers themselves nor outweighed by countevailing benefits to consumers or competition.[40]

The first prong of this proposed definition embodies fundamental common law principles and ensures full power in the FTC to prevent any and all instances of actual falsehood and intentionally misleading representations. Irrespective of any other consideration, lies and purposeful misrepresentation have no place in a well-functioning free market and are made subject to full FTC remedial authority.[41]

The second part of the Chambers's proposed statutory amendment would clarify the basic standards that the Commission should apply in evaluating allegedly "deceptive" acts that were undertaken unintentionally and in good faith. In such cases, the subsection requires that the practice "foreseeably result" in consumer injury in order to guide the Commission away from intuitive consideration of a statement's mere "capacity" to be misconstrued and towards a more objective inquiry as to whether consumers are reasonably likely to read the statement in a misleading sense.[42] This standard is also intended to prompt the Commission, in appropriate cases, to develop evidence, beyond its own subjective reactions and intuition, that consumers in fact perceive a double meaning.

The second part of the Chamber's proposal also contemplates that the meaning of an advertisement is to be that given it by the "reasonable" consumer.[43] It is intended to preclude the Commission from bringing enforcement actions, where the seller has acted in good faith, on the basis of an assumed misinterpretation by a consumer of particular carelessness or low intelligence. At the same time, this standard would preserve the law's current protection for members of particularly vulnerable groups to whom an advertisement may be specially targeted (such as children or senior citizens) and who therefore might be "directly" or "foreseeably" harmed and not reasonably able to avoid such harm. Advertising intended to deceive persons of whatever level of care or sophistication, of course, would be clearly barred under part (a) of the proposed definition.

Finally, the requirement of economic "injury" or detriment to the consumer in part (b) of the definition is intended to guide the Commission away from cases in which a claim made in good faith misleads a consumer, but the injury to the affected consumer or to consumers as a whole is slight. Thus, absent seller bad faith, the Commission would not institute proceedings where the market provides consumers with adequate self help and gives incentives to sellers to correct misimpressions. In addition, while a formal cost/benefit analysis is not required, the Chamber's proposed statutory standard would nonetheless prompt the Commission to consider whether the impact of a "deceptive" practice on some consumers is outweighed by the disadvantage of depriving other consumers who are not misled of useful, truthful information.

The final aspect of the Chamber's proposed definition of "deceptive" practices, which applies to both subparts, is the requirement that the claim at issue be "material."[44] This materiality requirement restores the commonly understood link between "deception" and actual selling practices. Only representations that relate to the qualities of the product or service that the seller is seeking to market and that influence the consumer's decision to buy the product should reasonably fall within the ambit of the "deception" doctrine.

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[40] Several other formulations of the second part or "injury" prong of the Chamber's proposed statutory clarification of the FTC's deception authority have been suggested in recent months. While the U.S. Chamber has not formally endorsed any of thes alternative proposals, we note that the language proposed by the advertising groups incorporates most of the key concepts in the Chamber's original draft as specifically applied in the "deception" context. That language is: (b) likely to mislead consumers, acting reasonably in the circumstances, to their detriment.

Because S. 2499 currently contemplates separate treatment of "unfairness" and "deception," the National Chamber recognizes that some modifications to its original proposal may well be appropriate.

[41] This first part of the proposed definition also preserves intact the legitimate core of the Commission's "substantiation" doctrine. A seller must have a good faith basis for making a claim at the time it is made or else he risks a finding or "reckless disregard" of truth or falsity. See National Dynamics Corp., 82 F.T.C. 488, 553 (1973), modified, 85 F.T.C. 391 (1975) in which the Commission articulated the substantiation concept as follows: "whether on the full record the substantiation constitutes a reasonable basis for the challenged claim."

[42] The alternative formulation cited in n. 40, supra, incorporates this same notion by use of the language "likely to mislead."

[43] Both the concept of "foreseeability" and the exclusion of alleged injury that is "reasonably avoidable" assume a "reasonable consumer" test. This same approach is included in the alternative formulation set forth in n.40 by means of the phrase "acting reasonably in the circumstances."

[44] The requirement that a representation be "material" is expressly included in the first part of the Chamber's proposal and is generally incorporated in the second part by the concept that the act or practice must "foreseeably result in substantial economic injury."

CONCLUSION

The Congress will certainly wish to give careful and detailed consideration to whether the Chamber's proposal, and alternative refinements of the concept, are a balanced remedy for the problems disclosed in the S. 2449 Report. These hearings are an important first step in this process, and the Chamber is prepared to work constructively with the Committee, its staff, and other interested parties to refine an appropriate definition. In the Chamber's view, however, the record of FTC activity and interpretation makes clear that the concerns previously expressed by the Committee are valid and that Congress can, and should, take action to remedy these problems within a reasonable time.

[The following information was subsequently received for the record:]

QUESTIONS OF THE COMMITTEE AND THE ANSWERS THERETO

Question 1. Several witnesses have suggested that current efforts to redefine the term "deception" will weaken the FTC's ability to protect consumers. For example, it is argued that the Chamber's legislative proposal will require very expensive and time-consuming consumer surveys in every deception case, thus crippling the FTC's ability to move quickly against fraudulent advertising claims. How do you respond to such criticisms?

Answer. The Chamber's proposal is not intended to, and would not, weaken the FTC's ability to protect consumers. Consumers are best protected when the FTC focuses its limited resources on acts or practices intended to defraud consumers or posing the risk of substantial consumer injury. Consumers are not well served when the FTC staff attempts to exploit the amorphous boundaries of "deception" or "unfairness" in broad rulemakings intended to regulate business practices the FTC finds distasteful, regardless of consumer interests. The Chamber's proposal is intended to clarify and strengthen the FTC's ability to deal with genuine market abuses while foreclosing further crusades of the Kid-Vid variety which are of far more interest to staff than consumers. Legislative action on these lines would both give the FTC meaningful priorities for enforcement and preclude further losses of public confidence through regulatory misadventure.

The contention that the Chamber's proposal would require surveys in all cases is a red herring. Where advertising claims are fraudulent—i.e., knowingly false or recklessly made—the Chamber's proposal would permit the FTC to take remedial action without regard to consumer impact. Consumer impact would be relevant only where an alleged misrepresentation was unintentional—i.e., not fraudulent. Even where consumer impact would be relevant, the Chamber's proposal does not specifically require survey evidence or any other form of proof. Impact may be obvious in some cases as where a critical element of product performance is misrepresented. In other cases, as where a misleading impression is allegedly conveyed by omission, more substantial proof of impact, like survey evidence, may be required. The Chamber believes that a realistic method of assessing consumer impact, evolved on a case-by-case basis, is a far better means of protecting consumers than current reliance on the subjective intuition of FTC Commissioners supposedly playing the role of careless or thoughtless consumers.

Question 2. How would the new statutory definition of "deception" that you propose affect the FTC's ad substantiation program? Please illustrate with examples.

Answer. The Chamber fully supports the concept that no advertiser should make affirmative product claims without having a good faith basis for them. The conduct element of the Chamber's proposed definition expressly incorporates this core substantiation concept. Moreover, the Chamber believes that, regardless of prior testing, an advertiser must be held responsible for substantial injuries inflicted upon reasonable consumers by claims which turn out to be false or misleading. The impact element of the Chamber's proposed definition incorporates this concept.

The Chamber's proposal would, however, limit two substantiation abuses which degrade the current conduct doctrine and which the Chamber believes are inconsistent with the Commission's own well reasoned opinion in National Dynamic Corp., 82 F.T.C. 488 (1973), modified, 85 F.T.C. 391 (1975). First, the Chamber's good faith approach would preclude the Commission from holding an advertiser responsible *per se* for failing to substantiate implied respresentations he did not know he was making. Second, the Chamber's proposal would preclude the Commission staff from making ex post facato pronouncements on the best available testing method. So long as the advertiser proceeded reasonably to substantiate the express and implied claims he intended to make, his advertising would be reviewed under the impact standard of the Chamber's proposal.

For example, assume that an advertiser claimed that laboratory tests showed his spot remover effective against oil stains but that he had no such tests or only sporadic, uncontrolled trials. Both the Chamber's proposal and current FTC doctrine would support a Section 5 violation without impact analysis.

But now assume that in making the same claim, the advertiser had furnished his product to a reputable laboratory which confirmed his belief. Under the Chamber's proposal, the advertiser could not be held liable under Section 5 unless the tests were wrong and the advertising caused the adverse impact set forth in the Chamber's impact standard. By contrast, current legal standards would allow the Commission to find implied representations as to the quality of laboratory work and the certainty of result. These implied representations could, wrongly in the Chamber's view, become a foundation for a substantiation violation even if the advertising were true. This is the flaw the Chamber seeks to correct.

Question 3. We have heard testimony that the FTC's "deception" powers are both well established in the case law and well understood by the advertising community. Is there really any need for Congress to tamper with the statutory definition of "deception" and, if we do so, won't we create more uncertainty by embarking upon uncharted waters?

Answer. It is true that, in a certain perverse sense, the FTC's "deception" powers are indeed "well established." As Senator Danforth observed during the 1979 FTC oversight hearings, "unfair and deceptive acts or practices, that is just whatever the FTC says it is," a non-standard where "the sky's the limit." Oversight of the Federal Trade Commission: Hearings Before the Subcomm. for Consumers of the Senate Comm. on Commerce, Science, and Transportation, 96th Cong., 1st Sess. 35, 36 (1979). Under current case law, the Commission has virtually unfettered discretion to interpret the "meaning" of an advertisement, using only its own "expertise," and to hold a seller liable for a hidden message that was never intended and that no reasonable consumer would perceive. Indeed, recent FTC decisions have so expanded deception analysis that it is today virtually indistinguishable from the Commission's much criticized and equally unbounded "unfairness" authority.

While the concept of unbounded FTC discretion may be well understood by the advertising community, it is not an effective guide to private conduct or FTC enforcement. It is clearly apparent that advertisers, and other businessmen, maintain a keen interest in the shifting views of FTC Commissioners and staff because the law is so amorphous. In those circumstances, we believe that a definition of "deception"—a concept now lacking any statutory content—is clearly a step in the right direction. This is particularly true of the Chamber's proposal which uses well-established legal conduct concepts and formulations on impact proposed by the Commission itself in the unfairness area. Rather than "embarking upon uncharted waters," legislative action of this type with respect to the FTC's deception powers would put an end to the confusion and uncertainty generated by oscillating enforcement policy and give consistent, meaningful guidance to the business community and reviewing courts.

Question 4. Are there any differences between the purpose and function of the common law tort of deceit on the one hand and FTC deception authority on the other?

Answer. Both the common law tort of deceit and FTC deception authority have the same fundamental purpose—namely, to protect the consumer from dishonest or reckless sales practices. Both are intended to be remedial in nature and to redress and deter specific consumer harm. While recent activist FTC proceedings might suggest differently, the Chamber does not believe that either the common law or FTC deception was intended as a regulatory tool to impose judicial/agency policy preferences on market practices or to control the content of commercial speech.

Common law tort and FTC deception procedures seek to achieve their basic consumer protection objective in slightly different ways. Under the common law, the plaintiff generally sues for financial relief and an award of monetary damages. FTC proceedings normally involve only injunctive relief prohibiting further deceptive acts and, perhaps, correcting past misrepresentations. While the common law thus contemplates that there will be sufficient injury to an individual consumer so as to justify invoking the judicial process, FTC procedures permit the agency to pursue and prevent deceptive practices based on aggregate impact on consumers as a whole, even though the injury to any single individual might be small. In this way, the remedial aspects of common law tort and FTC deception authority—though they function differently—complement each other in fulfilling their common purpose.

These comments comparing the common law tort of deceit and FTC deception practice, of course, reflect the Chamber's view of how Congress originally intended the FTC deception authority to operate. As described in detail in our July 22, 1982 testimony, expansive regulatory interpretations by the FTC over the years have so altered FTC deception doctrine that it now bears little resemblance to its common law roots. Indeed, the various problems and criticisms identified by this Committee in its report on S. 2499 all stem from the FTC's efforts to make FTC deception doctrine an independent legal approach—divorced from common law/common sense principles—under which the FTC can act affirmatively to "perfect" the flow of information according to its own notions of a properly functioning market.

Question 5. In what ways does your proposed statutory language differ from Chairman Miller's? Why? How does your proposal embody the requirement of reasonable interpretations of ad claims?

Answer. In both overall purpose and design, the Chamber's proposal and Chairman Miller's suggested statutory language are very similar. Both provide that misrepresentations made with improper intent are *per se* actionable on a misconduct theory. Similarly, both proposals recognize a need to bound enforcement efforts against unintentional misrepresentations made in good faith by requiring an appropriate analysis of injury to reasonable consumers.

The principal difference between the Chamber's position and Chairman Miller's articulation of "deception" is the degree of misconduct required to hold a seller strictly liable. In the Chamber's view, the conduct-oriented prohibitions of a new deception definition should apply where material statements are "known to be false or made in reckless disregard of their truth or falsity." Such a standard will deter unethical practices and fraudulent behavior, yet preserve legitimate freedom for commercial speech presented in good faith.

Chairman Miller's proposal would apparently apply a lower standard of simple negligence in assessing seller conduct under the deceptive per se analysis. To do so, we believe, goes further than necessary and cannot be justified under a conduct deterence rationale. Negligence is an elusive standard whose application would depend on the Commission's construction of a reasonable seller. In situations where seller bad faith is not in issue, the Chamber believes that a further analysis of actual injury to reasonable consumers is appropriate in order to justify FTC intervention against commercial speech.

The Chamber's proposed language, although perhaps not as explicit as Chairman Miller's, does embody a requirement of "reasonable" interpretation of ad claims. With respect to allegedly "deceptive" acts that were undertaken unintentionally and in good faith, the Chamber's draft requires that the practice "foreseeably result" in consumer injury and that such injury not be "reasonably avoidable." In this way, the proposed language would guide the Commission away from a purely subjective, intuitive consideration of a statement's mere "capacity" to be misconstrued and towards an objective inquiry as to whether consumers are reasonably likely to read or accept the statement in a misleading sense. There is therefore no difference, at least in intent, between the Chamber's and Chairman Miller's proposals with respect to the need for a "reasonableness" standard in interpreting the meaning of an advertising claim.

In this connection, we note that the Chamber's proposed statutory clarification of the FTC's consumer protection authority was originally advanced earlier this year as a means of providing parallel treatment for both "unfairness" and "deception." Because S. 2499 now contemplates separate treatment of these two concepts, the National Chamber recognizes that some modifications to its original proposal may well be appropriate and it is now carefully reviewing the thoughtful proposals that have been advanced by Chairman Miller and others. The Chamber stands ready to work with this Committee, its staff and other interested parties in refining draft language that best meets the overall objective of clarifying and rationalizing FTC "deception" doctrine.

Question 6. Why do you wish to limit deception to cases involving "substantial economic" injury? What does this mean? Why should the concept of injury be so limited?

Answer. The legislative language proposed by the Chamber would not limit FTC deception authority only to cases involving "substantial economic" injury. To the contrary, the Chamber's proposal fully preserves the FTC's ability to condemn and prevent knowing and reckless misrepresentations irrespective of whether or not any consumer injury has actually occurred. Lies, fraudulent misrepresentations and other forms of unethical advertising behavior have no place in a well functioning market and the Chamber's language would not place any limitation, injury related or otherwise, on the Commission's power to root out such practices.

The "substantial economic injury" requirement in the Chamber's proposal only comes into play in cases involving allegedly "deceptive" acts that were undertaken unintentionally and in good faith. In such situations of innocent misrepresentation, the Chamber adopts the same "injury" limitation that the Commission itself applies under its general consumer protection "Unfairness" jurisdiction. As the Commission made clear in its December 17, 1980 policy statement to Senators Ford and Danforth, "[u]njustified consumer injury is the primary focus of the FTC Act."

The Chamber's proposal includes the concept of "substantial economic injury" for the same basic reasons previously articulated in the Commission's 1980 policy statement (pp. 5–7). First, as a matter of enforcement priorities and given its limited resources, the Commission simply cannot afford to waste its efforts on "trivial or merely speculative harms." And second, as a matter of sound economic policy, the Commission "expects the marketplace to be self-correcting, and we rely on consumer choice—the ability of individual consumers to make their own private purchasing decisions without regulatory intervention—to govern the market."

Similarly, the Chamber believes that the 1980 policy statement also provides a reasonable definition of the meaning of "substantial" injury. As the Commissioners there explained, injury may be sufficiently substantial (1) "If it does a small harm to a large number of people" or (2) "If it raises a significant risk of concrete harm" to a smaller number of consumers. The Chamber's proposal would apply these same standards in "deception" cases where the seller has acted in good faith, thereby insuring that Commission resources are wisely spent and minimizing unnecessary regulatory intervention.

Senator KASTEN. Thank you, Mr. Rein.

Next, Mr. Mark Silbergeld who is the director of the Washington office of the Consumers Union. Mr. Silbergeld.

Mr. SILBERGELD. Thank you, Mr. Chairman.

I will submit my prepared statement for the record and summarize from it. An accompanying document, which I will also submit for the record, analyzes both the advertisers' proposed language to amend section 5 in order to define "deception" and the list of 19 cases that Chairman Miller sets forth as the basis for his proposal.

I did not at the time I prepared the testimony have the present version of Chairman Miller's proposed language, and I will be happy to submit an analysis of that as well for the record when I return my corrected transcript.

Senator KASTEN. Thank you. Your prepared testimony, as well as the additional documents that you referred to, will be made part of the record, and you may proceed with a summary.

Mr. SILBERGELD. Thank you, Mr. Chairman.

I would like to start by pointing out that the timing of the recommendation to define "deception" by statute itself is strong evidence that there is not a clearly understood and agreed upon problem with the lack of such a definition in the statute.

1980, as we all know, was open season on the Federal Trade Commission. Everybody that had a gripe stepped up and took their shots. Some of them I suppose were fair, and some of them were not, and some of them went somewhere and some of them did not.

But nobody can claim in 1980 that they did not have a chance to tell this committee and the comparable committee on the other side of the Hill what problems they had with the Federal Trade Commission.

We heard from neither any Commissioner nor, more importantly, from the advertising industry, a single peep about the lack of a definition of the term "deception 'in section 5 of the Federal Trade Commission Act.

My suggestion, quite frankly, is that it is both Johnny-come-lately and opportunistic. The definitions that are proposed, quite frankly my concern is not so much the difference between the language in the various proposals as the proposals themselves. They address no particular problem that has been clearly defined. Furthermore, contrivance of a statutory definition after 68 years of case law evolution and really 500 years of common law evolution of what is and what is not deceptive, and what principles are used to determine that, would create confusion and uncertainty rather than clear it up.

To take one example, we have to go back to the list that is claimed to justify or at least to illustrate the cases the Commission has brought that should not be deceptive under section 5. Chairman Miller cites the *Levitz* case. Well, I have no great argument that the *Levitz* case was the best allocation of resources the Commission could have brought at the time they brought that case. It was a local furniture store engaged in the kinds of practices that normally I would prefer to see State and local officials proceeding against. But though the chairman has analyzed that case as an example of why section 5 needs to contain a statutory definition of deception, he makes no mention of the deceptive initial contact doctrine, a very important concept in deceptive advertising law.

When we then look forward to the chairman's proposed language and the industry's proposed language, we are not told whether that language is intended to prevent the Commission from bringing a case such as *Levitz,* to prevent the Commission from bringing any case under the initial deceptive contest doctrine, or to the Commission from bringing that particular case without affecting that doctrine.

The lack of analysis to demonstrate what the problem is, if indeed there is a problem, is remarkable. And the lack of analysis to show how the proposed language affects a so-called problem is remarkable. I find it altogether remarkable that this committee is being asked to amend one of the major Federal consumer protection statutes now on the books without the sort of analysis that should accompany any such proposal.

The proposals create a number of other problems. As Commissioner Bailey pointed out, they could legalize deception by omission because of the particular way in which the proposed language has been drafted.

The proposed reckless disregard standard has no meaning in trade regulation law. It is more appropriately, and has been traditionally, used the initial penalty or liability is monetary. I do not think anybody proposing that language intends that to replace the cease and desist liability that now exists for most deception that the Federal Trade Commission can reach.

The proposed requirement for foreseeability of consumer injury is vague, and no one knows what consumer injury the statute would reach, let alone how to determine whether it was foreseeable by an advertiser.

The lack of definition of "injury" itself is perplexing. On the one hand, when we started off with Chairman Miller's list of cases, both the rerefined oil case and the foreign origin cases were criticized as cases the Commission should not have brought. Those were cases in which the consumer was injured because the consumer did not get what the consumer thought the consumer was getting.

Chairman Miller's argument was that the consumer got the value the consumer expected, and it was not the Commission's job, through application of the deception doctrine, to correct consumers' misimpressions about the effect of foreign origin or rerefining of oil on the quality of the product.

Now we hear through the press that Chairman Miller and Bureau Director Muris have done an about-face and they say consumer injury is when the consumer does not get what the consumer expects. So that it is not clear, if you adopted the language proposed, just what consumer injury is actionable under an amended section 5. And I suppose that would be the subject of extensive litigation.

I see my time is expiring, Mr. Chairman. There are other problems with the specific proposed language and any others likely to evolve will create. My prepared statement does identify those areas.

In closing, Mr. Chairman, I would simply urge that if this committee seriously entertains these kinds of amendments, that it should do so on the basis of a very rigorous analysis and not on the basis of the sort of half-baked proposals that have come forward so far, because they have failed to connect claimed problems and a claimed effective remedy on the existing body of law.

Thank you, Mr. Chairman.

[The statement follows:]

STATEMENT OF MARK SILBERGELD, DIRECTOR, CONSUMERS UNION WASHINGTON OFFICE

Mr. Chairman and Members of the Subcommittee, Consumers Union [1] thanks you for this opportunity to address the issue of Federal Trade Commission deceptive practices jurisdiction. The subject of your inquiry is very important to American consumers. It goes to the heat of business marketing practices. The proposals for Congressional consideration offered by the chairman of the Federal Trade Commission and by the advertising industry threaten the goal of honesty in the marketplace. We oppose any introduction in the Federal Trade Commission Act of a statutory definition of the term "deceptive."

Why at this late point in the Federal Trade Commission reauthorization process is the Congress inquiring into the meaning of the term "deception" as it appears in Section 5(a)(1), the key provision of the Federal Trade Commission Act? In 1980, the FTC underwent a firestorm of criticism from Congress and the advertising industry, among others. Most of that criticism was couched in such terms as "an agency run amok," "bureaucracy out of control" and "an agency meddling with social engineering." Whether these criticisms were right or wrong, the fact is that those subject to JTC jurisdiction had full opportunity to voice their criticisms of the agency. By and large, they convinced the Congress to limit the FTC's powers in those respects most troublesome to the agency's critics.[2]

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[1] Consumers Union is a nonprofit membership organization chartered in 1936 under the laws of the State of New York to provide information, education, and counsel about consumer goods and services and the management of the family income. Consumers Union's income is derived solely from the sale of Consumer Reports, its other publications, and films. Expenses of occasional public service efforts may be met, in part, by nonrestrictive, noncommercial grants and fees. In addition to reports on Consumers Union's own product testing, Consumer Reports, with over 2.8 million circulation, regularly carries articles on health, product safety, marketplace economics, and legislative, judicial, and regulatory actions which affect consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support.

It is significant that in 1980 nothing was heard from the advertising industry about the lack of a statutory definition of the term "deceptive" in Section 5. The first of this cry was not even heard from the industry. It came from the agency's new Bureau of Deceptive Practices, Director, Timothy Muris, then from its new Chairman, James C. Miller, III. Their criticism surfaced not in the form of an analysis and proposal but in the form of ad hoc criticisms of selected past FTC cases, many of them old and many of them improperly analyzed. And Chairman Miller did not include it in his prepared testimony before this Subcommittee at reauthorization hearings in March, but delivered it extemporaneously at the end of his prepared remarks. It took the FTC several days after the hearings to make public the list of cases to which he had referred. When Mr. Miller testified at House Reauthorization hearings in April, that list was subsequently updated to be more fully descriptive and to include more cases. Only then did Chairman Miller offer specific statutory language for Congressional consideration.

More significantly, only then did the advertising industry in general express support for the concept of defining "deceptive" by statute. And the industry's own proposed statutory language was not released until almost two weeks after the House hearings had concluded.

Mr. Miller and Mr. Muris are quite frank about the purposes that they believe a statutory definition of "deception" would serve. They feel that the Commission often has used its resources unwisely to litigate cases that either were unimportant to protection of consumers or actually injured consumers in such ways as limiting the availability of useful information. They believe, unwisely in my view, that such a definition would prevent the Commission from bringing cases they consider not to be sound.

The advertisers, I feel confident to assert, are less frank and explicit about their reasons for supporting such an amendment to Section 5. Consideration of such a proposal obviously creates an advantage for them in promoting the amendment in which they have the greatest interest, an exemption from the FTC's "unfairness" jurisdiction for commercial advertising, since serious consideration of a "deception" definition creates a tradeable item in the legislative process. Otherwise, it is difficult to understand why the industry wants to create the potential for a return to the kinds of advertising seen in the nation's media throughout the 1960's that lead to the revitalization of the FTC under President Nixon and to the FTC's flurry of legal action against deceptive advertising in the 1970's.

The Subcommittee should be mindful, as it entertains the plea to enact an untested definition of deception, that the advertising industry—at the same time it promotes this result—also urges Congress to exempt it from the FTC's "unfairness" jurisdiction, leaving "deception" as the only consumer protection standard to which it would remain subject.

On the merits, what is wrong with a statutory definition of deception? A great deal. In 1914 and 1938, when Congress enacted the Federal Trade Commission Act and the Wheeler-Lea Act, respectively, it decided not to define with particularity the specific business practices that would violate the law. Indeed, the very reason for creating a Federal Tade Commission was the recognition that Congress could neither foresee the infinite and ever-evolving way in which some businesses would act unscrupulously, nor could it rush to amend the statute every time such a practice was called to its attention. In its wisdom, Congress decided that only an expert Commission paying full-time attention to business practices could decide what practices would injure consumers and competition.

That wisdom is no less sound today. Further, since the meaning of the term "deceptive" has been defined on a case-by-case basis for the last sixty eight years, abandonment of the case law of deception, in favor of new statutory language not derived from case law, would create uncertainty, indeed the potential for chaos. Neither would consumers have any confidence that practices they reasonably consider to be deceptive would be unlawful under the new test, nor would the advertising industry and its legal counsel have any way to know what practices, long-since ruled to be unlawful or lawful under the deceptive practices doctrine, would remain so. If certain actions are deemed undesirable by society, it is appropriate to prohibit them specifically. But when what is undesirable is not the action but its actual or potential effect, then it is wiser to prohibit that effect. That is what the Congress did in 1914; it is understood by advertisers, their agencies and their lawyers. I doubt that the more difficult of advertising industry decisions about proposed advertising claims would be made any less difficult by a shift in the method of determining unlawfulness. These evaluations would, will if anything, become more uncertain.

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[2] It is a widely accepted myth that the FTC in the 1970's acted contrary to the expectations of the Congress. In fact, the agency merely got caught in a rather abrupt and drastic shift in those expectations as the composition of the Congress and of this Committee underwent change. See B. Weingast and M. Moran, "The Myth of the Runaway Bureaucracy—The Case of the FTC," Regulation, May/June, 1982, p. 33.

Nor is there any basis in Chairman Miller's case analysis for concluding that the current case-by-case method of defining deception produces serious FTC resources misallocation problems that would be cured by his or the advertisers' proposed statutory amendment. The cases he cites are mostly old and often he has poorly analysed them. I submit for the record my own critique of the nineteen cases Mr. Miller has cited to date as support for his argument. I believe that these analyses speak for themselves. (Interestingly enough, to date the industry proponents of statutory definition have not provided a list of cases or other evidence to support the argument that FTC has systematically misapplied the deception doctrine.)

Further, it is extremely curious that such responsible parties as the Chairman of the Federal Trade Commission and the leading trade associations of the advertising industry have urged the United Senate to cure a "problem" in the case law definitions of "deception" and have proposed language to define that term, but have utterly failed to offer any argument or analysis relating their proposed solutions to the claimed problem. If the Congress buys this "pig in a poke," it not only will fail to solve problems it mav believe to exist, but also will create substantial new problems in the process.

I have identified nine major issues raised by the amendment proposed by the American Advertising Federation, the Association of National Advertisers and the American Association of Advertising Agencies. There may well be others. I believe that a review of these problems is convincing evidence that a statutory definition of "deception" is unwise.

STATE LAW

First, the advertisers' proposal appears to seek avoiding any affect on "deceptive practices" jurisprudence under state Little FTC Acts. This can be concluded from the fact that their amendment limits the circumstances in which deceptive practices are unlawful, rather than defining the term "deceptive" as other proposals have done. But state law is likely simply to follow FTC case law development; it is unlikely that state courts will undertake an elaborate process of determining, in a case that FTC loses on appeal for failure to meet elements of such an amendment, whether FTC would have won under the now existing standard. At the very least, I urge you to consider carefully the views of the National Association of Attorneys General before accepting any representation by the advertisers that they have found a way to insulate state deceptive practices law from this proposed change in the federal law.

RECKLESS DISREGARD

This standard is one used in some criminal matters and as a standard for tort liability. There is no experience in applying it to marketing practices regulation. In the areas of law where it is utilized, monetary penalties or damages may be assessed for a first violation. Adopting it as a statutory standard for determining the lawfulness of deceptive acts or practices will give the Commission no guidance.

The advertising industry may argue that this standard will preserve the advertising substantiation requirement, which they support; but it would appear not to do so. The industry's argument is that making an objective performance claim without substantiation constitutes reckless disregard of the truth or falsity of the claim. But if the proposed standard is adopted, every advertiser will have some shred of substantiation in the file in order to avoid its application; indeed, there will be an incentive to develop bogus substantiation in order to avoid application of the standard. That will force the FTC to look at the quality of substantiation in many more cases than it does now.

DECEPTION BY OMISSION

The first test set forth in the advertisers' proposal (the knowing act or reckless disregard test) would only declare such acts or practices unlawful if the respondent made an affirmative material representation. It does not appear to apply to misrepresentation by material omission, even though deceptive advertising law doctrine clearly prohibits deception by omission and even though many important FTC decisions rest on the omission doctrine.

It is unclear why the advertisers think that they should be permitted to engage in knowing deception by omission of material fact or in deception by omitting material facts with reckless disregard for the effect of the omission on the truth or falsity of the advertising claim. They no doubt will point out that the FTC can deal with material omissions under the second test proposed by the advertisers. But there is no apparent reason why the Commission should have to prove substantial injury, having already proved that the advertiser has made a claim that omits a material fact with knowledge that it is material to the consumer's buying decision. This proposed standard would greatly increase the difficulty of proving the unlawfulness of deception by omission. The advertisers' motives for proposing this change should be closely examined.

MISREPRESENTATION

The second test proposed by the advertisers would reach "misrepresentation," rather than false representations. This appears to be a broader standard than the first test. But it does not explicitly reach all three of the categories of deception now reached by the present deception standard—falsity, misleading acts or practices and material omissions of fact.

FORESEEABILITY OF CONSUMER INJURY

At first blush, this element of the advertisers' second test appears to be intended to retain the "capacity to deceive" doctrine, which permits the FTC to conclude based on its own expertise that consumers may be injured by an act or practice without having to produce a "body count." But it is unclear on the face of the proposed amendment to whom the injury must be foreseeable—the actual advertiser, the FTC based on its own expertise, a reasonable advertiser, a reasonable person, a reasonable rugged individualist? This element typifies the kinds of legal questions that will be raised and subjected to endless litigation if efforts to codify standards for unlawful deception prevail.

SUBSTANTIALITY OF CONSUMERS' ECONOMIC INJURY

This element of the advertisers' proposed second test raises all of the questions raised by others' proposals to introduce benefit-cost evaluations into a definition of deception. What is substantial injury? Is it measured on a per customer basis or in the aggregage? Can the FTC act against a practice that deceives ten million people out of $4 each—or one that deceives four million people out of $10 each? Can it take into account how many other practices also impose small but measurable economic injury on a typical consumer?

How much harm per consumer constitutes substantial injury? Does the answer depend on whether most sellers of a relatively inexpensive item make the same deceptive claims, so that the consumer must incur the expense repeatedly in order to discover that the claim cannot be believed no matter which competitor makes it? Does the standard permit or require FTC to offset injury with benefit: if so, how does the FTC evaluate a few large injuries against many small benefits where there is a net benefit?

While the justification for adding an economic injury requirment to section 5 is to give FTC guidance in avoiding trivial cases, this and other standard to date proposed for that purpose introduce more uncertainty then they solve.

THE REASONABLE CONSUMER STANDARD

The advertisers' proposed second test would require FTC to show that the act or practice would injure a consumer who was "acting reasonably in the circumstances." As FTC Commissioner Bailey has suggested, that standard gives the Commission no guidance. What if fifty thousands Ph.D's are taken in by a practice that seems when described in the complaint to have been laden with signals to consumers not to be fooled? Is the Commissison restricted to evaluating the evidence as to the respondents' practices, or can it take the demographics of the "body count" evidence that enough "reasonable people" were fooled to establish that a "reasonable consumer" would be fooled? This element, also is justified by the asserted need to give the FTC guidance in avoiding trivial cases, but it creates many more questions than it answers—and makes the questions it raises litigable.

UNDERLYING JUSTIFICATION

Despite the fact that the 1980 FTC reauthorization process was "open season" on the agency, not a peep was heard from the advertisers about the need to address the "deception" concept of section 5. What has happened between 1980 and 1982 that the advertisers can point to as having created that need? What cases do they point to as justifying a statutory change in the "deception" concept and how do they relate specific cases on which they rely to the specific element they propose?

VIABILITY TO THE PROPOSED TESTS

Having proposed specific language to amend section 5, it would seem incumbent on the advertisers to demonstrate how their tests would fulfill the purpose for which they are offered. How do the advertisers claim their tests would apply to Chairman Miller's list of improvidently brought FTC cases—or to their own list? Are they prepared to make such a showing or do they expect the Subcommittee to accept their word that things will turn out right? Do they even have a list of cases they think to have been unwisely prosecuted by the FTC?

In conclusion, I would urge the Subcommitte that adoption of a statutory definition of "deception" is unjustified and should not become part of the legislation reauthorizing the Federal Trade Commission.

Senator KASTEN. Mr. Silbergeld, thank you. Next is Mr. Matthew Myers who is representing the Coalition on Smoking or Health.

Mr. MYERS. Mr. Chairman, my name is Matthew Myers. I appear today on behalf of the Coalition on Smoking or Health. The Coalition on Smoking or Health is an organization backed by the American Cancer Society, the American Heart Association, and the American Lung Association. And by 27 additional leading private health, education, and youth leadership organizations. On behalf of those organizations, I want to thank you and the members of the subcommittee for the opportunity to present my views on the current proposals and I want to urge you not to act to further alter the FTC's authority by redefining the Commission's deception jurisdiction until the need for change in the current legislation can be more adequately shown and the proposals now before you more carefully studied.

With regard to hazardous products such as cigarettes, the Federal Trade Commission has played an essential role in protecting consumers from advertising practices that are unfair and/or deceptive either because of specific statements made in those ads, or because the ads omit important health information about which consumers are not adequately informed. Had the FTC not acted over a decade ago, cigarette advertisements would carry no health warning, despite the overwhelming evidence of the health hazards of smoking.

Two points about the FTC's involvement with cigarette advertising bear emphasis. First, the FTC's most significant actions regarding cigarette advertising over the past two decades have focused on the omission of material facts relating to the health consequences of smoking rather than on specific false or deceptive statements in those ads.

Second, in each of these instances, the FTC's decision to act was based on its conclusion that cigarette advertising that failed to disclose material related information was unfair or deceptive. In none of these instances did the Commission rely solely on its jurisdiction over deceptive advertising.

Initially, therefore, it must be asked: What will be the effect of Congress decision to eliminate the FTC's unfairness jurisdiction? While a strong argument exists that the FTC can continue to require an effective health warning in cigarette advertisements under its current authority to regulate deceptive advertising practices, the answer is not clear. Until the full impact of eliminating the FTC's jurisidiction over unfair advertising is known, it would be dangerous to also narrow the FTC's deception jurisdiction.

A variety of proposals to narrow the FTC's deception jurisdiction have surfaced in recent months. Given the nature of these proposals, their impact could be dramatic. To illustrate, I would like to briefly explore the possible effects of a number of these proposals as they relate to cigarette advertising, and by analogy to advertisements for other hazardous products.

Senator KASTEN. Mr. Myers, right at that point before you begin that set, I am going to have to recess for a moment. We have 5 minutes to go with the vote that is occurring on the floor. I think we have a logical break right there.

Mr. MYERS. Fine, sir. Thank you.

Senator KASTEN. We will recess for one moment.

[Recess.]

Senator KASTEN. The committee will come to order. I would just like to apologize to all of you for the nature of the hearing today. It is difficult when you are competing with the tax bill on the floor. As you have seen, all of us have had to run back and forth for other kinds of things as well. But I am sorry it has been so disjointed, and I hope we can now continue through.

So, Mr. Myers, if you could pick up now on those examples that you were going to enumerate.

Mr. MYERS. Certainly, Mr. Chairman. I think it would be useful if I back up just one sentence so we can keep the train of thought.

As I said, a variety of proposals to narrow the FTC's deception jurisdiction have surfaced in recent months. Given the nature of these proposals their impact could be dramatic. I would like to give you a few illustrations.

First, several of these proposals would redefine deception to cover only material misrepresentations. This appears to mean that unless there is an affirmative material misstatement in the ad, the FTC would have no jurisdiction. If this requirement had been in effect in 1972, the FTC would not have been able to require a health warning on cigarette advertisements. If enacted, this requirement could undermine the authority of the FTC to require a health warning in any advertisement for a hazardous product simply because that ad failed to disclose the dangers of that product.

A second illustration: Several of the proposals would require the FTC to prove that the allegedly deceptive act caused direct consumer injury. According to the chamber's view, to meet this requirement the FTC would first have to prove that consumers would have made a different purchasing decision but for the deceptive misrepresentation. This means the Commission would have to prove that consumers purchased the product because of the deceptive statement and for no other reason; an extremely difficult burden. I shall explain.

The decision to smoke often is motivated by many factors. Studies show that among the reasons teenagers smoke is peer pressure and a desire to project an adult image. Cigarette advertising feeds into and associates smoking with these motivating factors, yet no one would say that cigarette advertising or the lack of health information in cigarette ads is the sole cause of a particular teenager's decision to smoke. Consequently, the first prong of the direct injury test, if adopted, probably could not be met in the case of cigarette advertising, and the FTC might not be able to require any cigarette health warnings at all.

There is a second prong to the proposed requirement that the FTC prove that the challenged deceptive activity directly causes consumer injury. Most of the proposals now before you would require proof of actual injury. The type of potential problem caused by this proposal is best demonstrated by an illustration from a matter now pending before the Commission.

Several cigarette manufacturers have alleged that Barclay cigarettes have a much higher tar content than the 1 milligram of tar which is the focus of its ads. In this case it is alleged that consumers are being deceived as to the tar content of the cigarettes being sold. However, the 1980 Surgeon General's report indicates that scientists are not certain whether the tar level differences at issue in this case are medically significant. If scientists cannot prove the medical significance of these allegedly false claims, can the FTC meet the proposed requirement? The answer is at best uncertain.

Third, several of these proposals would permit the FTC to exercise its jurisdiction only when the injury caused by the misrepresentation was not reasonably avoidable by consumers themselves. Does this mean that the availability of the annual Surgeon General's report on smoking or health frees the advertisers of cigarettes from their obligations to include a health warning in their ads? Given the language in the current proposals, this interpretation is not an unrealistic possibility.

Last, two proposals add an intent requirement to the definition of deception According to these proposals, it would not be enough to show that an advertisement was deceptive or false or that it omitted material health information. The FTC would also have to prove that the advertiser knew that the advertisement was false.

Does this mean cigarette advertisers could advertise that there are no known health hazards associated with smoking? After all, twice this year a leading tobacco industry executive has testified before congressional committees to this fact. I can only assume he believes that. The FTC should be able to stop false and deceptive advertising without regard to what the advertiser believes.

This discussion of the potential impact of a number of the pending proposals is designed to demonstrate the potential implications of these proposals. A change of this magnitude should not be undertaken without a thorough and thoughtful study.

Thus, on behalf of the Coalition on Smoking or Health, I ask you to take no action on the pending proposals to redefine the FTC's deception jurisdiction unless and until it can be determined that the change is in the public interest and the proposed changes will not harm consumers.

I would just like to add one brief point to my written testimony. Congress is now considering a bill, S. 1929, which would replace the current health warning with a system of disease-specific potentially more effective health warnings. The action already taken by this committee with regard to the unfairness jurisdiction of the FTC and the adoption of any of the proposals now pending before this committee concerning deception makes it substantially more important that Congress itself make a statement on the need for health warnings, rather than leaving this matter solely to the discretion of the Commission.

I thank you.

[The statement follows:]

STATEMENT OF MATTHEW L. MYERS. COALITION ON SMOKING OR HEALTH

Mr. Chairman, my name is Matthew L. Myers. I am a partner in the law firm of Asbill & Junkin, but appear today on behalf of the Coalition on Smoking OR Health. The "Coalition on Smoking OR Health" is an organization backed by twenty-seven of the nation's leading private health, education and youth leadership organizations, including the American Cancer Society, the American Heart Association and the American Lung Association. The Coalition serves as the public action arm of the National Interagency Council on Smoking and Health, and was created to bring smoking prevention and education issues to the attention of legislators and federal officials and to promote support for federal smoking prevention education programs. I want to thank you and the members of the Subcommittee for the opportunity to present my views on the current proposals to adopt a more detailed, statutory definition of the phrase "deceptive acts or practices" as used in Section 5 of the Federal Trade Commission Act.

On behalf of the Coalition I want to urge you not to act to further alter the F.T.C.'s authority to act to protect consumers pursuant to Section 5 of the Federal Trade Commission Act by redefining the Commission's "deception" jurisdiction, until the need for change in the current legislation can be more adequately shown, the proposals now before you more carefully studied and the full impact of the decision to prohibit the Commission from regulating commercial advertising on the basis that the advertising constitutes an "unfair act or practice" more fully evaluated.

The Federal Trade Commission has played an essential role in protecting consumers from advertising practices for hazardous products, such as cigarettes, that are unfair and/or deceptive either because of specific statements made in or images and associations created by these ads or because these ads omit important health information about which consumers are not adequately informed. Given the overwhelming evidence of the health hazards caused by cigarette smoking, the American public has a right to be well informed about the health hazards of smoking. Had the F.T.C. not acted over a decade ago, cigarette advertisements would carry no health warning. Had the F.T.C. not examined the effectiveness of the current health warning last year, there would be no meaningful debate today about the need for a more effective system of health warnings. Both actions by the Federal Trade Commission have contributed substantially to the public's increased awareness of the health hazards of smoking and both, therefore, have contributed significantly to the overall public welfare. Thus, the Coalition is concerned about any proposal which will make it more difficult and may make it substantially more difficult for the F.T.C. to continue to provide this protection for consumers. It is for this reason that the Coalition opposes the proposed changes in the F.T.C.'s deception jurisdiction. To appreciate our concern, it is useful to briefly review the history of the F.T.C.'s involvement with cigarette advertising.

BRIEF HISTORY OF F.T.C. INVOLVEMENT WITH CIGARETTE ADVERTISING

Cigarette advertising has been a concern of the Federal Trade Commission since the late 1930's when the Commission sought to prevent cigarette companies from making unsupported claims about the medical and other benefits of particular brands.[1] Between 1945 and 1966, the Commission issued seven (7) cease and desist orders prohibiting various false claims in cigarette advertising.[2] Unsubstantiated representations about the "tar" and nicotine content of certain cigarette brands prompted the Commission to seek and obtain agreement from cigarette manufacturers to eliminate these deceptive claims from their advertisements as long ago as 1960.[3]

The modern era of the Federal Trade Commission's concern about cigarette advertising began not quite 20 years ago. In 1964, following the issuance of the Report on Smoking and Health of the Advisory Committee to the Surgeon General,[4] the Federal Trade Commission found that the mounting evidence of the "grave hazards to life and health" caused by cigarette smoking, together with the failure of the cigarette manufacturers to warn consumers of this danger, constituted "an unfair or deceptive act or practice" (emphasis added) within the meaning of Section 5 of the Federal Trade Commission Act.[5] At that time the Commission concluded that if consumers did not know about the health risks of smoking, cigarette advertising which failed to disclose these dangers was unfair or deceptive.

The Trade Regulation Rule promulgated by the Commission in 1964 would have required all cigarette packages and advertisements to disclose clearly and prominently that cigarette smoking is dangerous to health and may cause death from cancer and other diseases.[6] In 1965, Congress pre-empted the F.T.C. action by enacting legislation requiring all cigarette packages distributed in the United States to include the statement: "Caution: Cigarette Smoking May Be Hazardous To Your Health." [7] In addition, the 1965 Cigarette Act prohibited the F.T.C. from requiring any other disclosure requirements on the cigarette package, and precluded, until July 1, 1969, any government requirement of a disclosure regarding smoking and health in cigarette advertisements. As the congressionally mandated moratorium neared its conclusion in mid-1969, the Commission proposed a modified version of the 1964 Rule. Instead, however, Congress then amended the message on cigarette packages to read: "Warning: The Surgeon General Has Determined That Cigarette Smoking Is Dangerous To Your Health." [8] Neither the 1965, nor the 1970 Acts required a health warning in cigarette advertisements and none were placed in cigarette ads voluntarily by cigarette manufacturers. Two years later, in 1971, the F.T.C. announced its intention to file complaints against the cigarette companies, alleging that advertising without a disclosure that smoking is dangerous to health would be "false and misleading" and would constitute an "unfair practice." Lengthy negotiations between the Commission and the six major cigarette manufacturers culminated in 1972 in consent orders requiring cigarette advertisements to display clearly and conspicuously the same warning that Congress already had required on cigarette packages.[9]

Only last year the Commission issued a new report on cigarette advertising.[10] In this Report, the Staff of the Commission found that while the past efforts of the Commission and the Congress to increase the amount of health information available to consumers have had a positive effect, the problems which prompted the Commission to act in the past still exist. The data examined by the Commission's staff indicated that although most Americans are generally aware that smoking is hazardous, many consumers do not have enough information about the health risks of smoking in order to know how dangerous smoking is, i.e., what is the nature and extent of the health risk of smoking. The data also indicated that many consumers do not know whether the general health risks of smoking have any personal relevance to themselves or whether they are among those groups of people who may be uniquely vulnerable to these health hazards.[11]

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[1] Julep Tobacco Co., 27 F.T.C. 1637 (1938); Green River Tobacco Co., 27 F.T.C. 1547 (1938).

[2] R. L. Swain Tobacco Co., 41 F.T.C. 312 (1945); P. Lorillard Co., 46 F.T.C. 735, order modified, 46 F.T.C. 853, aff'd., 186 F.2d 52 (4th Cir. 1950); R. J. Reynolds Tobacco Co., 46 F.T.C. 706 (1950), modified, 192 F.2d 535 (7th Cir. 1951), on remand, 48 F.T.C. 682 (1952); American Tobacco Co. 47 F.T.C. 1393 (1951); Philip Morris & Co., Ltd., 49 F.T.C. 703 (1952), vacated and remanded on motion of Commission, complaint dismissed on affidavit of abandonment, 51 F.T.C. 857 (1955); Liggett & Myers Tobacco Co., preliminary injunction denied, 108 F.Supp. 573 (S.D.N.Y. 1952), aff'd mem., 203 F.2d 955 (2d Cir. 1953), decision of Commission, 55 F.T.C. 354 (1958); Brown & Williamson Tobacco Corp., 56 F.T.C. 956 (1960) (consent order).

[3] 2 Trade Reg. Rep. (CCH) ¶7853.51.

[4] U.S. Department of Health, Education and Welfare, Smoking and Health: Report of the Advisory Committee to the Surgeon General of the Public Health Service (1964) ("1964 Surgeon General's Report").

[5] The Trade Regulation Rule for the Prevention of Unfair or Deceptive Advertising and Labeling of Cigarettes in Relation to the Health Hazards of Smoking, 29 Fed. Reg. 8324, 8325, 8326 (July 2, 1964). ("The 1964 Cigarette Rule").

[6] The 1964 Cigarette Rule at 8324, 8325, 8326.

[7] Federal Cigarette Labeling and Advertising Act ("Cigarette Act"), 15 U.S.C. §§ 1331 et. seq. (1965).

[8] 15 U.S.C. §§ 1331, et. seq. (1970).

[9] Lorillard, et al., 80 F.T.C. 455 (1972).

[10] Federal Trade Commission, Staff Report on the Cigarette Advertising Investigation, May 1981.

The Commission's Report further noted a continuing special concern about the need for cigarette advertisements to be accurate and complete in disclosing the health risks of smoking because of their hazardous nature,[12] because of the fact that cigarette advertising may adversely affect particularly vulnerable groups of consumers, such as pregnant women, individuals who suffer from cardiovascular or chronic obstructive lung disease and teenagers, and because any deception in cigarette advertising is aggravated by the continuous and massive amount of cigarette advertising to which the American public is and has been exposed. The Commission recognized that the total impact of prolonged and voluminous advertising may exacerbate any misimpression created by the advertising because repeated exposure to a large number of ads that extol virtues of a product without disclosing its specific negative consequences may cause consumers to ignore those negative facts.[13]

Two points about the F.T.C.'s past involvement with cigarette advertising bear emphasis. First, the Federal Trade Commission's most significant actions regarding cigarette advertising over the past two decades have focused on the omisssion of material facts relating to the health consequences of smoking rather than on specific false or deceptive statements in these ads. Second, in each of these instances, the F.T.C.'s decision to act was based upon its conclusion that cigarette advertising that failed to disclose material health related information was or may have been "unfair or deceptive." In none of these instances did the Commission rely solely on its jurisdiction over "deceptive" advertising.

IMPACT OF CONGRESSIONAL ACTION ON UNFAIRNESS ON THE CURRENT DECEPTION PROPOSALS

Therefore, it must be asked: What effect will Congress decision to eliminate the F.T.C.'s "unfairness" jurisdiction over commercial advertising have on its ability to monitor and regulate cigarette ads which fail to adequately disclose the health hazards of smoking. The answer is not certain. While a strong argument exists that the F.T.C. can continue to require an effective health warning in cigarette advertisements under its current authority to regualte "deceptive" advertising practices,[14] its ability to do so has not been reviewed by the Courts in recent years. Until the full impact is known of requiring the F.T.C. to limit its regulation of commercial advertising for hazardous products, like cigarettes, to those ads which are found to be "deceptive" as that term is currently used, it would be dangerous to further narrow the F.T.C.'s "deception" jurisdiction. Further Congressional action at this time could result in a situation in which consumers would have no protection against ads which fail to disclose serious and substantial health hazards.

Is this concern justified? Recently, Stanley Cohen, the well-respected columnist for Advertising Age wrote, in discussing the impact of the proposed changes to the F.T.C.'s jurisdiction:

Here's an example, cited by one to Chairman Miller's people: As this newcomer sees it, the "old" commission stretched "deception" to cover health hazard warnings in cigarette ads, when in fact the absence of health hazard information ought to be regarded only as "unfair". The newcomers hope to insert language to restrict the use of "deception". But suppose Congress also exempts all advertising from "fairness". Goodby cigarette health warnings." [15]

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[11] Id.

[12] National Commission on Egg Nutrition, et al., 88 F.T.C. 89, 162 (1976), modified, 570 F.2d 157 (7th Cir. 1977), cert. denied, 439 U.S. 821 (1978); Firestone Tire and Rubber Co., 81 F.T.C. ( ), aff'd., 481 F.2d 246 (6th Cir. 1973), cert. denied, 414 U.S. 2112 (1973); 1964 Cigarette Rule, supra.

[13] *Warner-Lambert Co.* v. *F.T.C.*, 562 F.2d 749) (D.C. Cir. 1977); see, *Waltham Watch Co.* v. *F.T.C.*, 318 F.2d 28 (7th Cir. 1963), cert. denied, 375 U.S. 944 (1963); *Royal Baking Powder* v. *F.T.C.*, 281 F. 744 (2d Cir. 1922); 1964 Cigarette Rule, supra, at 8356–8357. See also *The J.B. Williams Co.* v. *F.T.C.*, 381 F2d 884, 890 (6th Cir 1967).

[14] See, Federal Trade Commission Staff Report on the Cigarette Advertising Investigation , at 4-17 et seq.

[15] Cohen, Stanley, "Washington Beat", Advertising Age, June 28, 1982, p. 26.

Similarly, in the March 25, 1982 Memorandum to Chairman Miller, cited in the Hearing Record on S. 2499,[16] from Timothy Muris, the current Director of the F.T.C.'s Bureau of Consumer Protection, Mr. Muris questions the wisdom of the Commission requiring effective warnings on cigarette advertisements pursuant to its "deception" jurisdiction.

The legislative history of S. 2499 on this point is also unclear. While the Committee Report indicates that ads that depict the unsafe or unlawful use of an otherwise safe or healthful product still can be brought under a "deception" theory because they fail to reveal material facts, the Committee Report does not explicitly authorize the use of the F.T.C.'s "deception" jurisdiction to prevent the advertising of products whose normal usage is hazardous if those ads fail to reveal material health information about the advertised product.[17]

We are certain that Congress did not intend to expose consumers to this health risk or to deprive consumers of their right to be informed about the health hazards of smoking by deciding to remove the F.T.C.'s jurisdiction over "unfair" advertising, but we are concerned that any further narrowing of the F.T.C.'s jurisdiction over advertising at this time could have that unintended result.

IMPACT OF CURRENT DECEPTION PROPOSALS

A variety of proposals from a variety of sources to narrow the F.T.C.'s "deception" jurisdiction have surfaced in recent months. While many proposals have been suggested, none have been thoroughly studied. Yet, given the nature of many of these proposals, their impact on consumers, the business community and the F.T.C. could be dramatic. Before Congress acts, it is essential that the need for and impact of these changes be carefully studied to avoid creating a gaping hole in the protection provided to and needed by consumers and business.

To illustrate, I would like to brefly explore the possible effect of a number of these proposals as they relate to cigarette advertising and, by analogy, to advertisements for other hazardous products.

First, several of these proposals would redefine deception to cover only "material misrepresentations." This appears to mean that unless there is an affirmative material misstatement in the advertisement, the F.T.C. would have no jurisdiction. If this requirement had been in effect in 1964 and 1972, the F.T.C. would not have had jurisdiction to require a health warning in cigarette advertisements. If enacted, this requirement could undermine the authority of the F.T.C. to require any advertisement for a hazardous product which failed to disclose the dangers of that product from being required to carry a health warning unless the ad falsely and explicitly stated that the product was safe.

Second, several of the announced proposals would require that the F.T.C. prove that the allegedly "deceptive" act caused direct consumer injury. This simple sounding requirement has serious potential implications. According to the Chamber of Commerce and the National Association of Manufacturers, to meet this requirement the F.T.C. would first have to prove that consumers would have made a different purchasing decision but for the deceptive misrepresentation. This means the Commission would have to prove that consumers purchased the product because of the deceptive statement and for no other reason: an extremely difficult burden in most cases and a virtually impossible burden for cigarette advertising or for advertisements of other hazardous products which fail to reveal material health information. I shall explain.

Typically, cigarette advertisements contain few affirmative statements of any kind. Instead, they often seek to associate smoking with an image with which people wish to identify or emulate, especially young people. Thus, ads for Marlboro focus more on the Marlboro man than on Marlboro cigarettes. Virginia Slims ads focus on the modern liberated, sexually attractive woman more than the cigarette. How could the F.T.C. prove that a consumer purchased cigarettes because of these ads and these ads alone? In addition, cigarette advertising is not the sole reason a person starts smoking. The decision to smoke often is motivated by many factors. Several studies show that among the reasons teenagers smoke is peer pressure, the desire to appear "cool" and the desire to project an adult image. cigarette advertising feeds into and associates smoking with each of these motivating factors. Yet, no one would or could say that cigarette advertising or any particular cigarette ad or, even the lack of health information in cigarette ads, is the sole cause of a particular teenager's decision to smoke. Consequently, the first prong of the "direct injury" test, if adopted, probably could not be met and the F.T.C. might find itself powerless to require any cigarette health warnings at all if this requirement were adopted.

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[16] Reauthorization of the F.T.C., Hearings before the Commerce, Science and Transportation, United States Senate, Ninety-Seventh Congress, Second Session. March 18 and 19, 1982, at 57, 59.

[17] Senate Report No. 97–451, Federal Trade Commission Amendments Act of 1982, 97th Congress, 2d. Session, March 28, 1982.

There also is a second prong to the proposed requirement that the F.T.C. prove that the challenged deceptive practice directly causes consumer injury. Even if the F.T.C. can prove that consumers relied and acted upon the challenged deceptive practice, most of the proposals now before you would require proof of actual injury. The type of potential problem caused by this proposal is best demonstrated by two illustrations from matters now pending before the Commission. In one, several cigarette manufacturers have alleged that Barclay cigarettes have a much higher "tar" content than the one milligram of "tar" which is the focus of its ads. In short, they allege that the statements about "tar" content in the Barclay ads are false. In the second illustration, one cigarette company has alleged that three of its competitors are engaging in deceptive advertising practices by promoting a very low "tar" line of a popular brand while generally making available only a look-alike higher-tar cigarette of the same brand. In both cases, it is alleged that consumers are being deceived as to the "tar" content of the cigarettes being sold. However, the 1980 Surgeon General's Report indicates that scientists do not know whether the "tar" level differences at issue in these two cases are medically significant. The evidence in future years may prove that the "tar" levels in question are medically important, but today we cannot answer that question with reasonable scientific certainty. If scientists cannot prove the medical significance of these allegedly blatent, false claims, can the F.T.C. meet the proposed requirement that the deceptive practice directly cause injury? The answer is, at best, uncertain.

Third, several of the proposals would permit the FTC to exercise its jurisdiction only when that the injury caused by the misrepresentations were not "reasonably avoidable by consumers themselves." Does this mean that the availability of the annual Surgeon General's Report on Smoking or Health which is available to members of the public frees the advertisers of cigarettes from their obligation to include health warning in their ads or to deal with the smoking and health issue accurately. Given the language in the current proposal, this interpretation is not an unrealistic possibility.

Fourth, two proposals carefully limit the scope of the F.T.C.'s jurisdiction to "economic" injury. Do these proposals seriously intend to divert attention away from physical injury or serious emotional distress? If so, they should be rejected out of hand.

Last, two proposals add an "intend" requirement to the definition of deception. According to these proposals, it would not be enough to show that an advertisement was deceptive or that it omitted material health information, the F.T.C. also would have to prove that the advertiser knew that the ad was false or acted in reckless disregard for the truth. Twice this year a leading tobacco industry executive has testified before Congressional Committee to this fact. I can only assume he believes it. Does this mean that cigarette advertisers could advertise that there are no known health hazards associated with smoking with the knowledge that the F.T.C. would be powerless to intervene? The F.T.C. should be able to stop false and deceptive advertising without regard for what the advertiser believed.

This discussion of the potential impact of a number of the pending proposals for narrowing the F.T.C.'s "deception jurisdiction" is not intended to be all-inclusive or to be the final authoritative statement of the subject. Instead, it is designed to demonstrate the potential implications of these proposals. Change of this magnitude should not be undertaken without a thorough and thoughtful study to avoid unintended results of serious consequence for the American consumer. Thus, on behalf of the Coalition on Smoking or Health, I ask you to take no action on the pending proposals to redefine the F.T.C.'s "deception jurisdiction" until it can be determined that change is in the public interest and that the proposed changes will not harm consumers or the public health.

Senator **Kasten**. We thank you, Mr. Myers. Next is Mr. Paul Daniel, representing Brown & Williamson Tobacco Co.

Mr. **Daniel**. Thank you, Mr. Chairman. I have submitted a short statement and will only say here that we have appeared before this committee previously in urging the committee to restrict the Federal Trade Commission's authority to regulate nondeceptive advertising on the vague and ill-defined ground of fairness, and are pleased that the committee has incorporated such provisions in the pending authorization bill.

We do not see any similar need for legislation defining deception for the reasons that have been stated here before by Commissioner Bailey and others; that we do not see that the term is vague and uncertain, and it does have a well-defined meaning, established in many cases over many years that people can rely on.

I would want to point out just a couple of things; that there is no linkage in our mind between fairness and deception. And there is no peril to the cigarette health warnings. There have been a couple of references to that this morning.

I should point out that the health warnings that appear on all cigarette packages are mandated by legislation, and the warnings in advertising are carried pursuant to a consent order agreed to between the Commission and the industry members in 1972. And they are carried there by virtue of that, which has the force and effect of law. And that 1972 consent order was just, 1 year ago, incorporated in a consent judgment of the U.S. District Court for the Southern District of New York, and it is a firm law. And there is no issue of Commission discretion in regulating, so that is established. I do not believe the proposals that are being advanced here today would have any effect one way or another on that.

I know of no movement to alter that circumstance.

I would only address one other question. I think Mr. Myers inadvertently misspoke when he suggested that cigarette advertising associates smoking with teenage peer pressure. Cigarette advertising does not feature teenagers or young people in any way, shape or form, never has, and I do not believe ever would, even if all regulation were eliminated tomorrow.

But essentially our position is, as others have stated, we do not see the need for this form of legislation on the subject of deception.

[The statement follows:]

STATEMENT OF PAUL DANIEL ON BEHALF OF BROWN AND WILLIAMSON TOBACCO CO.

My name is Paul Daniel. I am a member of the Washington, D. C. law firm of Kaler, Worsley, Daniel & Hollman and am submitting this statement on behalf of our client, Brown & Williamson Tobacco Corporation of Louisville, Kentucky.

I understand that the purpose of this hearing is to examine the suggestion of Chairman Miller that the Federal Trade Commission Act be amended to incorporate a new definition of deception. I am familiar with Chairman Miller's general suggestion, but I am not aware that it has been reduced to legislative language and so I do not know precisely how an amendment of the sort he favors might be drafted and what all its effects might be.

Our principal interest in connection with the regulation of advertising concerns the provision in S. 2499 restricting the Federal Trade Commission's ability to regulate non-deceptive advertising on the vague and undefinable grounds of unfairness. The Commission has exercised authority to regulate deceptive advertising since the FTC Act was passed in 1914, and I believe there is an overwhelming consensus that that is a necessary and desirable authority. By and large, at least until now, the Commission's exercise of that authority has not been a source of great controversy.

However, the Commission's unprecedented assertion in recent years of authority to regulate the content of non-deceptive advertising on the broad, almost limitless grounds of unfairness contains substantial potential for mischief and abuse. It raises serious concerns on constitutional grounds as well as on grounds of regulatory policy. We are pleased, therefore, that the Committee has recommended restriction of that authority in S. 2499.

We are not convinced of the need for the kind of changes Chairman Miller has suggested on the subject of deception. They deal with a basic authority which the

Commission has exercised since the beginning, the scope and limits of which have been defined in large numbers of cases before the Commission and the courts. To amend this authority now and introduce new concepts and terminology into a familiar statute would be likely to introduce needless uncertainty into an area of the law that has until now been pretty well settled. Therefore, we do not feel that we can endorse the Chairman's proposals on deception at this time.

We believe that those proposals have been overly simplified and too hastily devised. For example, I have seen no discussion of how the proposals would or would not affect the Commission's authority to regulate deceptive practices as unfair methods of competition, a traditional authority which existed long before the word "deceptive" appeared in the statute. for another thing, the so-called Bumper's Amendment, the subject of pending legislation, would alter the standards for judicial review of agency action and with will eliminate one of the major arguments made in support of Chairmen Miller's proposals, namely, excessive judicial deference to the Commission's "expertise."

For these reasons, we think the Chairman's proposals deserve more careful consideration and analysis, and need to be formulated with more precision as specific legislative proposals before we could determine a firm position on their merits.

Senator KASTEN. Mr. Daniel, thank you very much for your testimony.

The final witness of this panel is Mr. David Versfelt, representing the American Association of Advertising Agencies, accompanied by Mr. Gilbert Weil and Mr. William Rogal.

Mr. Versfelt.

Mr. VERSFELT. Thank you, Mr. Chairman. I will speak in the prepared testimony for the American Association of Advertising Agencies [four A's], the American Advertising Federation [AAF], and the Association of National Advertisers [ANA]. Mr. Gilbert Weil for the ANA and Mr. William Rogal for the AAF, both seated directly behind me, will be available to respond to questions.

Mr. Chairman, these three advertising groups are the national trade associations which together represent the overwhelming majority of the people and companies comprising the ad industry in America. We are testifying today in an attempt to assist this committee to explore concerns that have been raised about the scope and use of the FTC's authority over deceptive advertising. We refer you to the written statement which we have filed today which elaborates in detail the points that I will make herein, and I would request that that be filed in the record.

Senator KASTEN. Without objection, your additional materials will be filed in the record.

Mr. VERSFELT. The Commission's regulatory mandate over "deceptive acts and practices" fully warrants the serious attention afforded by this hearing. The act as presently written provides little guidance regarding what kinds of initiatives the Commission should undertake. Consequently, much internal agency effort is expended in trying to determine whether a particular case should be brought. Once brought, the Commissioners have little, if any, guidance as to how the case truly should be decided.

As Professor Rosden states in his treatise on the law of advertising:

> It has been said sometimes, and not without a measure of truth, that an advertisement is deceptive if the Federal Trade Commission calls it so. This situation, unusual as it is in American jurisprudence, is due to a combination of reasons. In the first place, Congress has not seen fit to set legislative standards that have an ascertainable degree of definiteness.

The result has been an unstructured and often aimless series of agency undertakings that too often restrict advertising without any showing that the ads are in fact misleading or harming consumers.

When such agency restrictions occur in the area of commercial speech, the principles of the first amendment are infringed—not only the right of the advertiser to communicate but also the rights of those who would receive the communication to have the benefit of the information it would contain. The first amendment mandates that the free flow of advertising information not be restricted in the absence of a showing that the representation is inherently misleading or has actually misled.

We offer today a statutory formulation that we believe is faithful to these fundamental principles. Let us emphasize, however, that we are not wedded to any particular words, provided that whatever language is ultimately agreed upon recognizes the first amendment principles at stake.

Our formulation is this: Deceptive acts or practices should be declared unlawful when they consist of either, one, material representations known to be false or made in reckless disregard of their truth or falsity; or—and I emphasize that it is an or there—two, misrepresentations that directly cause or may foreseeably result in substantial economic injury to consumers acting reasonably in the circumstances.

The first clause of our provision addresses advertising known to be false or in reckless disregard of the truth. Such advertisements should not be countenanced. In our view, when a claim is made without substantiation, that is reckless conduct. So this clause establishes what might be described as a "per se" category that would permit the Commission to challenge the ad without regard to whether the claims have caused any injury to consumers. We believe this first provision will clarify and therefore strengthen the Commission's position vis-a-vis false or unsubstantiated advertising.

The second clause of our proposal provides the Commission with a further authority to challenge advertisements even where the advertiser has acted in good faith. In such cases the Commission could nonetheless act if the ad contained a misrepresentation that might cause substantial economic injury to consumers acting reasonably under the circumstances. In measuring substantial injury we intend that the Congress permit the Commission to aggregate injuries of affected consumers. By "acting reasonably in the circumstances," we intend to permit introduction of a rule of reason in the interpretation of the advertisements. Hopefully, this will end the situation of having the Commission find an ad deceptive by interpreting it in a way that no one else does. Significantly, this "in the circumstances" test would permit the Commission to afford special protection to vulnerable groups by allowing it to evaluate an advertisement's capacity to deceive in reference to the audience's orientation and motivation.

We hope we have made clear, Mr. Chairman, that we are not seeking to protect advertisers who might disseminate false or deceptive advertisements. Nor are we seeking to curtail ad substantiation, which should require that an advertiser insure that claims made in its ads be substantiated by support such as would satisfy a reasonably prudent advertiser as to their truth.

Clearly, we are not seeking to weaken consumer protection from injury due to false, deceptive, or misleading ads. Rather, we offer this proposal in the form of statutory language in an attempt to assist this committee in exploring concerns of principle that have been raised about the deception authority of the Commission.

We believe that our formulation provides a definition of Commission, authority that will help to clarify the constitutional requirements and congressional purposes that must govern responsible regulation of advertising.

We remain eager to assist the committee, the Commission, or any other interested parties in any way we can in further study of this matter in the time ahead.

Thank you, Mr. Chairman.

[The statement follows:]

JOINT STATEMENT OF THE AMERICAN ADVERTISING FEDERATION, THE AMERICAN ASSOCIATION OF ADVERTISING AGENCIES AND THE ASSOCIATION OF NATIONAL ADVERTISERS

This statement is respectfully submitted jointly by the American Advertising Federation (AAF), the American Association of Advertising Agencies, Inc. (A.A.A.A.) and the Association of National Advertisers, Inc. (ANA), national trade associations which together represent the overwhelming majority of all persons and companies which comprise the advertising industry in America. We submit this statement in an effort to assist this Committee to explore concerns that have been raised about the scope and use of the Federal Trade Commission's authority over deceptive advertising. In compliance with the request of the Chairman and the Committee staff, this statement is limited to the issue of the Commission's "deception" authority. Other important issues relating to the Commission's authority under the Federal Trade Commission Act are addressed in submissions we have made to this Committee earlier this year.

IDENTIFICATION OF THE ASSOCIATIONS

The AAF is a national trade association which includes within its membership all of the various elements of the advertising industry. Its principal office is located at 1225 Connecticut Avenue, Northwest, Washington, D.C. 20036. The membership fo the AAF includes companies which manufacture and sell consumer products, advertising agencies, newspaper and magazine publishers, radio and television broadcasters and networks and approximately 22 other trade associations with memberships composed of companies engaged in various advertising pursuits. The Federation also represents the "grassroots" of the advertising industry because it is the parent body of more than 200 local advertising clubs and federations located throughout the United States and having a combined membership of approximately 25,000 advertising practitioners. These local organizations, like the parent body, include advertisers. advertising agencies and media within their membership.

The A.A.A.A. is the national association of the advertising agency business. Its more than 540 members, both large and small, are located throughout the United States and handle approximately 75 percent of all national advertising placed by advertising agencies in this country. Its address is 666 Third Avenue, New York, New York 10017 and it maintains a Washington office at 1899 L Street, Northwest, Washington, D.C. 20036.

ANA is a not-for-profit corporate trade association, organized and existing under the laws of the State of New York with offices at 155 East 44th Street, New York, New York 10017. It is composed of approximately 400 companies located throughout the United States which manufacture and sell a wide range of products and which employ advertising as an important element of their marketing and public relations programs. Although ANA's membership includes many of the nation's largest advertisers, it also includes a large number of smaller ones. Approximately one-third of ANA members spend under $1 million annually for advertising. The common characteristic of all ANA members is that they purchase space and time from the media of mass communications.

INTRODUCTION

Before we explain our concerns, it is important that we point our some of the things we are not trying to accomplish.

We are not seeking to weaken consumer protection from injury due to false, deceptive or misleading advertisements. Nor are we seeking to reduce prompt and effective prosecution by the Federal Trade Commission in appropriate cases. Although we believe the FTC has on occasion been overzealous in seeking to enjoin "deceptive" advertising,[1] claims or statements that constitute harmful misrepresentations cannot be countenanced in our industry. We recommend that Congress explicitly clarify its intent that the First Amendment, which guarantees everyone freedom from unwarranted abridgement of commercial speech, shall be conscientiously observed as the Commission goes about its regulatory activities.

We are not seeking to affect the FTC's power to require that positive claims made in advertisements must be substantiated by and based upon factual support in the possession of the advertiser such as would satisfy a reasonably prudent advertiser as to their truth. We believe that such positive claims as "get 14 percent better performance" or "9 out of 10 people prefer" clearly represent to the consumer that the advertiser has conducted tests or surveys or has some other basis for making the statements in good faith. That implication is false, i.e., "deceptive," if the advertiser in fact lacks such material.

Finally, we are *not* seeking to destroy or weaken the FTC. Insofor as advertising is concerned, we believe that a national regulatory body is needed. But our industry is acutely aware that the FTC has in the recent past over-stepped the boundaries of its congressional mandate, requiring that Congress reaffirm its insistence upon the principles of the First Amendment and proper administrative regulation.

ADVERTISING IS SPEECH PROTECTED BY THE FIRST AMENDMENT, SO THE FEDERAL TRADE COMMISSION'S AUTHORITY TO REGULATE OR PROSCRIBE "DECEPTIVE" ADVERTISING MUST BE CLARIFIED

Our democracy and our marketplace are grounded upon the conviction that wise decisions are most likely to be made when a broad range of information is disseminated. The First Amendment thus protects the free flow of information. Communication does not take place without a receiver as well as a sender, so the right of all to speak freely implies an equal right on the part of the public to hear those who would speak. Indeed, the freedom to learn, to be fully informed on matters of interest, is as precious an inheritnace as the freedom to tell.

Therefore, the guarantees of the First Amendment reach beyond the individual speaker to encompass, as well, the recipient of the communication. As the Supreme Court summarized in a case which invalidated as unconstitutional a Virginia statute prohibiting the advertising of prices of prescription drugs, "[i]f there is a right to advertise, there is a reciprocal right to receive the advertising." *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 757 (1976). See *Red Lion Broadcasting Company* v. *FCC*, 395 U.S. 367, 390 (1969); *Stanley* v. *Georgia*, 394 U.S. 557, 564 (1969); *Martin* v. *Struthers*, 319 U.S. 141, 149 (1943). While the persuasive aspect of commercial advertising may be of particular value to seller of goods or services, the informational content is no less significant to consumers, whose knowledge of product availability and attributes would be restricted in the absence of advertising. The public's understanding varies with the quantity and quality of its information. As a consequence, the Supreme Court's decisions involving corporations which have undertaken to communicate with a segment of the public are appropriately based: not only on the role of the First Amendment in fostering individual self-expression but also on its role in affording the public access to discussion, debate, and the dissemination of information and ideas.

First National Bank of Boston v. *Bellotti*, 435 U.S. 765, 783 (1978) (footnote omitted) (citing cases).

We submit that under Constitutional principles, commercial speech—advertising—cannot be restricted or proscribed unless a court[2] determines that it is deceptive, or that the resolution directly serves a substantial governmental interest and does not exceed what is necessary to serve that interest. As the Supreme Court has explained in the context of advertising for professional services,

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[1] Cases abound in which the Commission has revealed an ability to overreach in pursuing the business of censoring. E.g., Kroger Co., D. 9102 (Sept. 25, 1981); Ford Motor Co., 87 F.T.C. 756 (1976); Spiegle, Inc., 82 F.T.C. 20 (1973), 494 F. 2d 59 (7th Cir.), cert. denied, 419 U.S. 896 (1974); Standard Oil Co., 84 F.T.C. 1401 (1974), modified, 577 F. 2d 653 (9th Cir. 1978).

[2] See *Blount* v. *Rizzi*, 400 U.S. 410 (1971).

> Commercial speech doctrine . . . may be summarized generally as follows: Truthful advertising related to lawful activities is entitled to the protections of the First Amendment. But when the particular content or method of the advertising suggests that it is inherently misleading or when experience has proven that in fact such advertising is subject to abuse, the states may impose appropriate restrictions. Misleading advertising may be prohibited entirely. Even when a communication is not misleading, the state retains some authority to regulate. But the state must assert a substantial interest and the interference with speech must be in proportion to the interest served. *Central Hudson Gas Co.* v. *Public Service Comm'n* 447 U.S., at 563-564. Restrictions must be narrowly drawn, and the state lawfully may regulate only to the extent regulation furthers the state's substantial interest.

In the Matter of R.M.J., 102 S. Ct. 929, at 937-38 (1982) (footnote omitted).

Consequently, we respect and endorse the suggestions made by a number of concerned individuals and organizations that the FTC Act include an explicit definition of what constitutes a "deceptive act or practice." The need for such a definition has also been pointed out by Professor Rosden in his treatise The Law Of Advertising:

> It has been said sometimes, and not without a measure of truth, that an advertisement is deceptive if the Federal Trade Commission calls it so. This situation, unusual as it is in American jurisprudence, is due to a combination of reasons. In the first place, Congress has not seen fit to set legislative standards that have an ascertainable degree of definiteness. Nor has Congress written standards into the Act after several decades of administrative and judicial ad hoc interpretations. Section 18.03, p. 18-46 to 18-47.

Timothy Muris, the Director of the Commission's Bureau of Consumer Protection, has also endorsed the need for clarification of the Commission's overbroad and unconstrained authority to censor advertisements as deceptive. In a memorandum filed on April 1, 1982 with Chairman Miller's Separate Statement before the House Subcommittee on Commerce, Transportation and Tourism, Mr. Muris concluded:

> Because the current Section 5 legal standard is so broad and ambiguous, case selection has been a time-consuming and recurrent problem. Because the Commission can do almost anything, the question has always been what should it do? Ideally, a body of law should clearly characterize a central core of transactions that will always result in liability.
>
> Throughout its controversial 68 year history, the FTC has never quite fulfilled its promise of providing consistent and substantial protection to consumers. The fault lies not in the fine people who have served here, but instead in the overly broad standards that Congress has provided us—standards that do not provide guidance on how to proceed. With these broad standards, in one era the Commission did little, focusing largely on trivia. In the next, the Commission took upon itself the mantle of the second most powerful legislature in America, surely a task inappropriate for five unelected officials. Muris Memorandum, at 26-27, 29.

In other words, the unbounded discretion left with the Commission in the area of "deception" leaves the agency unguided—and unaccountable—as to what Congress and the public want it to do, and not to do. The result has been an unstructured and often aimless series of agency undertakings that too often rescrict advertising without any showing that the ads are in fact misleading or harming consumers. Without specific statutory language, there can be no real understanding of the Commission's proper purposes.

THE COMMISSION SHOULD NOT BE LEFT UNBRIDLED AND THUS ABLE TO IGNORE THE CONGRESSIONAL MANDATE THAT REGULATORY ACTIVITY BE IN THE PUBLIC INTEREST

Our prior comments to this Committee, as with our statement today, propose a statutory formulation for the Federal Trade Commission Act. Nonetheless, let us emphasize at the outset that we are not wedded to any particular words, provided that whatever articulation might be chosen achieves our fundamental purposes. In this matter our principles are our objectives.

From its enactment, the Federal Trade Commission Act has unequivocally voiced a congressional intent that public and private resources not be wasted on regulatory activities that are not required to serve the public interest. E.g., FTCA § 5(b), 15 U.S.C. § 45(b): ". . . and if it shall appear to the Commission that a proceeding by it . . . would be to the interest of the public . . ." While the courts in recent years appear to have adopted something of a hands-off policy regarding the particulars of Commission decisions to issue complaints, see *FTC* v. *Standard Oil Co.,* 449 U.S. (1980), the principle nevertheless survives that administrative initiatives must legitimately further public policies or goals. As the Supreme Court made clear in *FTC* v. *Klesner,* 280 U.S. 19, 28 (1929): "To justify filing a complaint the public interest must be specific and substantial." [3] The Commission and the courts must give more than lip service to the concept that the federal government should avoid pursuit of trivia and concentrate on matters which are material consequences of intentional or reckless behavior or which otherwise significantly harm consumers.

In an attempt to provide a particular statutory formulation that we believe will satisfy the principles we explain today, we offer the following provision:

Deceptive acts or practices in or affecting commerce are declared unlawful where such acts or practices—(1) consist of material representations known to be false or made in reckless disregard of their truth or falsity, or (2) consist of misrepresentations that directly cause or may forseeably result in substantial economic injury to consumers acting reasonably in the circumstances.

This formulation is the one proposed by us in Supplemental Testimony to this Committee submitted on April 20, 1982 and in our Joint Statement to the House Subcommittee on Commerce, Transportation and Tourism dated April 22, 1982.

The portion of this formulation which has attracted the most attention is the first subclause, which would make unlawful any material representations "known to be false or made in reckless disregard of their truth or falsity"—regardless of whether the representations caused or were likely to cause consumer injury. Critics assert that this sub-provision could inject into the FTC Act a standard akin to that applicable to common law libel and, they assert, might make it difficult for the Commission to mount successful challenges to misleading advertising. Nothing could be farther from the truth. This first subclause will actually clarify the Commission's position with respect to false advertising by affirming the Commission's authority to pursue such challenges even without a finding of consumer injury.

The advertising industry has always believed that advertising known to be false or recklessly unsubstantiated should not be countenanced by the Commission regardless of its lack of injurious impact on consumers.[4] As we have stated on previous occasions, and we reiterate today, an advertiser and its agency must ensure that positive claims made in their advertisements are substantiated by and based upon support such as would satisfy a reasonably prudent advertiser as to their truth. Failure to meet that standard of conduct, in our view, constitutes reckless behavior.

The second subprovision of our proposed formulation provides the Commission with an additional authority to challenge advertisements when the advertiser has acted without knowledge that its representation is false and without having failed to obtain reasonable substantiation. In such situations, the Commission would nonetheless be able to challenge the advertising if it contained misrepresentations that (1) caused or might foreseeably result in substantial economic injury to consumers who were (2) acting reasonably in the circumstances.

This subclause of our proposal does not require that the economic injury to each and every consumer be substantial in order to support a Commission initiative. On the contrary, as the Supreme Court set forth in *FTC* v. *Klesner*, supra, injury that is "substantial" enough to satisfy the requirements of the public interest may be based on an aggregate of injuries to affected consumers.

Sometimes, because, although the aggregate of the loss entailed may be so serious and widespread as to make the matter one of public consequence, no private suit would be brought to stop the unfair conduct, since the loss to each of the individuals affected is too small to warrant it. 280 U.S. 19, 28 (1929).

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[3] In too many instances over the years, the courts have allowed the Commission to pursue cases where the injury was either trivial or non-existent. This hands-off attitude of the lower courts is best exemplified by the First Circuit's opinion in *Colgate-Palmolive Co.* v. *FTC*, 310 F.2d 89 (1962), second opinion, 316 F.2d 517 (1963), rev'd on other grounds, 380 U.S. 374 (1965), a case that involved a television advertisement which the Commission charged was deceptive because it illustrated that an application of the respondent's shaving cream would enable one to shave sandpaper. In the words of the Court:

> It may well be that little injury was done to the public by respondent's representations. We suggested in our opening sentence that we consider this a rather trivial case. Nevertheless, we could not possibly say that it was not within the province of the Commission to conclude that such conduct should be forbidden.

310 F.2d at 92. The fact that some courts have felt powerless under the current statute to prevent expenditure of time and money on trivial cases is a powerful argument for clarifying the Act.

[4] Significantly, the Commission has for some time now been operating on a principle less demanding upon advertisers than the one we propose here, a principle that the marketplace for "low ticket" items is "self-correcting." As we understand it, this means that the Commission will not proceed in an advertising case when the advertised goods are low in cost, frequently purchased and the consumer can judge for himself or herself whether the products live up to the claims made for them. See 1975 FTC Policy Protocol: Deceptive and Unsubstantiated Claims. In such situations, the theory goes, the consumer will quickly shift his purchasing choice to another product and the problem will be corrected by operation of the market.

Indeed, the Commission itself has confirmed that the public interest standard should control in regard to measuring the extent of injury. In the Commission's Decmber 17, 1980 letter to Senators Ford and Danforth of this Committee, the first requirement for Commission initiation of a challenge under a part of Section 5 of the Act was stated as follows:

First of all, the injury must be substantial. The Commission is not concerned with trivial or merely speculative harms.[5]

We see no reason why, in this regard, our proposal should be interpreted as a significant departure from the Commission's present stated policy.

Our proposal would also direct the Commission to rely on (and authorize reviewing courts to consider) whether the advertisements may foreseeably mislead consumers "acting reasonably in the circumstances." At present, the courts are virtually precluded from questioning a Commission decision that an advertisement has an undefined quality described as "capacity to deceive" the public. In the words of one court, "The meaning of an advertisement to the public and whether it is calculated to deceive is a question of fact, and the Commission's conclusions with reference thereto may not be disturbed unless arbitrary or clearly wrong."*Gulf Oil Corp.*. v. *FTC*, 150 F. 2d 106, 108 (5th Cir. 1945). Such a simplistic rule has resulted in orders restricting advertising representations where there had been no showing that even unthinking, ignorant, or highly credulous consumers could have been misled. E.g., *FTC* v. *Mary Carter Paint Company*, 382 U.S. 46 (1965); *FTC* v. *Colgate-Palmolive Co.*, 380 U.S. 374 (1965); *Spiegel Inc.* v. *FTC*, 494 F. 2d 59 (7th Cir.), cert. denied, 419 U.S. 896 (1974); *Prima Products, Inc.* v. *FTC*, 209 F.2d 405 (2d Cir. 1954); *Gelb* v. *FTC*, 144 F.2d 580 (2d Cir. 1944).

Our proposal would merely affirm that something akin to a rule of reason should be a part of the process of interpreting advertisements in Commission cases. The courts would continue to bear the duty to review a Commission finding as to the deceptive nature of an advertisement, and to affirm the Commission's findings if they are supported by substantial evidence, but in doing so they would be permitted to evaluate whether the evidence relied upon by the Commission supported a finding that reasonable consumers were likely to be misled.[6]

It is important to note, however, that our proposal is carefully worded to afford special protection to vulnerable groups. The language "acting reasonably in the circumstances" is intended to protect such groups by permitting that an advertisement's capacity to deceive be evaluated in reference to the audience's orientation and motivation.

The advertising industry is convinced that any criticism leveled at its position on deception is based upon a misunderstanding of the specific legislative language we are proposing. The Committee might ask why it would be "impossible" for the Commission to prove that a misrepresentation "may foreseeably result" in injury to consumers. What is so "revolutionary" about a requirement that advertising statements be interpreted as reasonable consumers would interpret them? What is so "reasonable" about holding an advertisement unlawful based only upon an unreasonable reading of it.[7] We are confident that the answers to these and other questions will demonstrate the worth of our formulation.

CONCLUSION

We offer this proposal in the form of statutory language in an attempt to assist this Committee in exploring concerns of principle that have been raised about these aspects of the Commission's authority. We believe that our formulation provides a definition of Commission authority that will help to clarify the Constitutional requirements and congressional purposes that must govern responsible regulation of deceptive advertising. At botton, however, our concern remains with the principles we have explained today and in prior statements to this Committee.

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[5] An injury may be sufficiently substantial, however, if it does a small harm to a large number of people, or if it raises a significant risk of concrete harm.

[6] Here again, we are not attempting to inject an unprecedented standard into Commission decisionmaking. In *Aronberg* v. *FTC*, 132 F.2d 165, 167 (7th Cir. 1942), the Court said:

The ultimate impression upon the mind of the reader arises from the sum total of not only what is said but also of all that is *reasonably* implied. (Emphasis added.)

A few years later, in *P. Lorillard Co.* v. *FTC*, 186 F.2d 52 (4th Cir. 1950), a Court held:

In determining whether advertising is false or misleading . . ., regard must be had, not to fine spun distinctions and arguments, that may be made in excuse, but to the effect which it might *reasonably* be expected to have upon the general public. (Emphasis added.)

[7] See, e.g., Kroger Co., D. 9102 (Sept. 25, 1981) (ads for "Price Patrol" found deceptive despite Commission concession that their claims of lower prices were basically true), *Gelb* v. *F.T.C.*, 144 F.2d 580 (2d Cir. 1944) (ad for "permanent" hair coloring found deceptive because some consumers might think "permanent" meant "forever effective with only one application").

Finally, the Committee's announcement of this hearing described it as a "first step" in a systematic review of this subject, and we are pleased with that description of the Committee's commitment to a thorough and thoughtful examination. We remain eager to assist this Committee, the Commission or other interested parties in any way we can in furthering the study of this matter in the time ahead. With this affirmance of our continuing interest, we greatly appreciate the opportunity afforded the advertising community to present its views on this important subject.

[The following information was subsequently received for the record:]

AUGUST 26, 1982.

Senator ROBERT W. KASTEN, Jr.,
Chairman, Committee on Commerce, Science, and Transportation,
Washington, D.C.

DEAR SENATOR KASTEN: The American Advertising Federation, the American Association of Advertising Agencies, Inc. and the Association of National Advertisers, Inc. are pleased to respond to your request of August 5, 1982 for answers to four questions posed by the minority members of your Subcommittee with respect to proposals to amend section 5 of the Federal Trade Commission Act to define the word "deceptive". As our testimony before your Committee reveals, we strongly support a clarifying amendment to prevent recurrence of past abuses by requiring that the Commission bring proceedings, either rulemakings or complaints, only when a substantial public interest is served thereby. The minority has raised questions with respect to the anticipated effect of the proposed amendments, and we now turn to our responses to their inquiries.

1. The first question is: You testify that each consumer need not suffer substantial injury—that injury to consumers may be aggregated. Chairman Miller has testified that deceptive ads concerning cheap products, subject to repeat purchase and with claims easy to verify should not be prosecuted. Would you agree where many consumers have been deceived?

In the first place we are not certain that the question correctly states Chairman Miller's present position. He has not stated that the disseminators of deceptive ads concerning cheap products subject to repeat purchase and capable of easy verification by consumers "should not be prosecuted", but only that the Commission should carefully evaluate such situations to determine whether a proceeding is justified. In fact, Chairman Miller is not the originator of this concept. It is one of the criteria in an FTC staff directive entitled "Deceptive and Unsubstantiated Claims Policy Protocol" which has been in effect since 1975. This "protocol" is designed to guide the FTC's staff in the preparation of deceptive advertising complaint recommendations to the Commission.

While we do not dispute the concept that market forces may have a corrective effect on deceptive advertising in some cases we do not endorse it as a shield for deliberately deceptive or unsubstantiated advertising. After all, we must assume that the advertiser who knowingly chooses to use deception is also aware of corrective market forces but has decided that the advantages of deception outweigh the disadvantages of long-run consumer disillusionment. Such deliberately false advertising should not be permitted. Chairman Miller's legislative proposal would permit the Commission to take action without regard to the effects of an advertising practice when it can be shown that the advertiser knew or had reason to know that his advertisement was misleading. The proposal of the advertising groups contains a similar provision, although in slightly different words.

2. The second question posed by the Minority is: What effect does the Miller proposal have on "deception by omission"?

As we interpret Chairman Miller's proposal it will have no effect at all upon the concept of "deception by omission". While it is true that Chairman Miller's definition would appear to require a "material representation", we interpret this to mean only that the advertisement must be "misleading in a material respect".

In our view most of the Commission's abuses in the area of required affirmative disclosures have not been founded upon alleged deception but upon alleged unfairness to consumers. This undue arrogation of power over commercial speech will not be corrected by amending the deception standard alone, but will require eliminating the Commission's power to proscribe advertising on grounds of unfairness. Amendment of the deception standard is needed but standing alone it is only a half measure. Full protection for the constitutional rights of advertisers and consumers can only be achieved by enactment of all proposals we have made.

3. The third question is: Several witnesses have suggested that current efforts to redefine the term "deception" will weaken the FTC's ability to protect consumers and unleash a flood of unethical and fraudulent practices? How do you respond to such criticisms?

Nothing could be farther from the truth. We have yet to see any basis for these criticisms of the proposals. The critics are long on rhetoric but short on facts or even hypothetical instances illustrating the verity of their predictions. The only matters which couldn't be reached if the deception standard was amended as proposed would be trivial, inconsequential matters which do not involve a substantial public interest. In view of the obvious need for priorities, why should the Commission ever proceed against an advertisement which is not knowlingly false or which will not injure a reasonable person? When these elements are lacking there is a clear absence of public interest, a statutory prerequisite for Commission proceedings which has too often been ignored.

Finally, it must be remembered that these proposals do not constitute wholesale changes in the law which would make a large number of heretofore unlawful practices unassailable. In essence, only two categories of federal proceedings would be eliminated by the proposals, the trivial and those based upon an unreasonable interpretation of an advertising message.

4. The fourth question is: If a seller makes a false claim concerning a product that costs 88 cents, the individual consumer has little economic injury. But assume that due to the false claim, these products are sold to millions of consumers as a first purchase—and competitors are substantially harmed by loss of sales, should the FTC have authority to police this action? Why or why not?

What if in this example, one competitor is driven out of business?

Of course, under our proposal the Commission need not even reach the question of economic injury to consumers or competitors if it can show that the advertiser knew the claim was false or made the claim in reckless disregard of its truth or falsity.

But the question poses a situation in which "competitors are substantially harmed by loss of sales" and poses, hypothetically, a situation in which the harm is so extensive that "one competitor is driven out of business." Thus, we assume that the Minority would like our views as to the effect of our proposal upon the Commission's ability to protect competition from deceptive practices.

The response to that aspect of the question is rather simple. None of the legislative proposals would affect in any way the Commission's right to continue to bring cases charging that false advertising constitutes an "unfair method of competition." It has successfully brought advertising cases under that provision of Section 5 since as early as 1919. The only limitation upon the Commission's authority to bring a proceeding under that provision of the statute is the same limitation which applies in all cases, i.e., there must be "specific and substantial" harm to the public interest. *FTC* v. *Klesner*, 280 U.S. 19 (1929).

Moreover, competitors have a surer and swifter means than government action to protect themselves. First, a competitor can sue for an injunction and damages under Section 43(a) of the Lanham Act, 15 U.S.C. § 1125(a), for false advertising. E.g., *Vidal Sassoon, Inc.* v. *Bristol-Myers Co.*, 661 F.2d 272 (2d Cir. 1981) (shampoos); *McNeilab, Inc.* v. *American Home Products Corp.*, 501 F.Supp. 517 (S.D.N.Y. 1980)(OTC analgesics). Second, a competitor can avail himself of the self-regulatory machinery of the advertising industry, the National Advertising Division of the Council of Better Business Bureaus and the National Advertising Review Board.

There are many reasons why these remedies should be preferred over the FTC. Competitors will be able to make their own expert judgments about whether a claim is false or deceptive; they will know whether a deceptive claim is having a perceptible effect in the marketplace; they can proceed on their own motion without waiting for FTC review and authorization of a complaint. These mechanisms are working well and will continue to do so.

We hope that we have fully responded to the Committee's inquiries. We will be pleased to supply additional comment or information if needed.

Respectfully submitted,

William W. Rogal,
General Counsel for American Advertising Federation
David S. Versfelt,
Counsel for American Association of Advertising Agencies, Inc.
Gilbert H. Weil,
General Counsel for Association of National Advertisers, Inc.

Senator **Kasten**. Mr. Versfelt, thank you very much.

Because of the time and also because of the complex nature of this particular issue, we are going to submit questions to you for the record. It is particularly significant, I think, that we have a Miller proposal which is different from the chamber proposal, which is even somewhat different from the advertiser's proposal.

I think we will want to examine all these different proposals, as well as the objections from Mr. Silbergeld and others.

I would like to just thank all of you for your testimony, for your participation here, and to say that we will be back in touch with all of you with additional questions as we further seek to define this problem.

Thank you for your participation.

Mr. **Versfelt**. Thank you, Senator.

Mr. **Rein**. Mr. Chairman, could I ask formally that our written presentation be included in the record of the hearing? I neglected to do that.

Senator **Kasten**. We will do that. Next will be Mr. Calvin Collier.

Mr. Collier.

STATEMENT OF CALVIN COLLIER

Mr. **Collier**. Mr. Chairman, my name is Calvin Collier. It is a delight to be back before this committee. It has been many years.

Senator **Kasten**. Mr. Collier, we thank you for your patience.

Mr. **Collier**. It has not been many years this morning. It has been many years since I have been here.

I especially appreciate this opportunity to share with you my personal views on proposals that have been made to provide some legislative guidelines to the term "deceptive" as it is used in the FTC act.

I have prepared a statement for the committee and have submitted it for your consideration. I hope it will be included in the record.

Senator **Kasten**. It will be included in the record, and we appreciate your willingness to excerpt and comment from your statement.

Mr. **Collier**. That is my intent. In the next few moments I shall try to summarize the contents of my statement.

Congressional attention to the FTC's stewardship of the deception standard under current law is both timely and overdue. As my testimony points out, the Commission and the courts have been largely, indeed almost exclusively, responsible for this essentially legislative task during the 44 years since Congress inserted the word "deceptive" into section 5.

Under these judicial and agency interpretations that term has been greatly expanded. As a result, the Commission is presently empowered to prohibit representations that do not harm consumers and that in fact actually benefit the great majority of them. Moreover, the problem is not simply one of excess Commission authority. By and large the Commission has used its sweeping power with commendable restraint.

It is not my purpose to revisit four decades of individual decisions or to second guess their wisdom. Rather, I would like to address the legal standards that have evolved to give deception its substantive content. Congress should keep in mind that these standards, and not simply the Commission's application of these standards, is the law of the land.

In the words of the statute, it is unlawful to commit deceptive acts or practices as those terms have been defined by the FTC and the courts. In my view, Congress has an obligation to review the controlling interpretations of deception and provide the courts and the agency with some fresh guidance on its scope and meaning.

Chairman Miller has commendably shared with you his reservations regarding the overbreadth of existing doctrine and presented a carefully tailored set of legislative proposals to modify the law.

My prepared testimony describes in detail the doctrines that would be modified by the Chairman's suggestions, as well as many of the doctrines that would not. I have also attempted to describe the practical effects of these changes and the policy considerations that support them.

These proposals, which I join in recommending to you, would, in a nutshell, define deception as a material representation either that is likely to mislead consumers acting reasonably in the circumstances to their detriment, or that the respondent knew or should have known was false. In essence, these standards would abandon those precedents under existing law which impose liability without regard to the reasonable reactions of consumers, the reasonable conduct of the advertiser, or the lack of any probable injury to consumers.

I do not support legislation because the Commission is in the habit of abusing its existing authority. I support it because the Commission's generally reasonable approach to deception, which usually conforms to the proposed standards, deserves some permanence. In my view, the lack of meaningful standards contributes to gamesmanship by advertisers who must guess where the lines will be drawn between the overbreadth of existing doctrine and the shifting majority of the Commissioners. The deficiency also contributes to gamesmanship by the Commission staff to whom existing legal doctrine provides very little or no legal guidance.

The proposed changes to the statute are selective and based on well-known legal principles. Neither the Commission nor the courts would have any difficulty in applying them. Inevitably, the debate over the standards that the Commission uses or should use is somewhat metaphysical. Any words that might be used to prohibit the evils of deception without unduly impeding the flow of useful commercial information will inevitably possess an elastic quality. Precision here is unattainable. With or without changes in law, the factfinder in those cases will be required to consider the evidence and exercise sound judgment.

Under current doctrine, as well as these proposals, the Commission will retain the primary responsibility to determine whether deception has occurred, and the role of the reviewing courts will be restrained and limited.

In my view, the proposed standards are superior to existing standards for several reasons. They eliminate the conflict between announced doctrine on the one hand and the more reasonable application of it by the Commission on the other.

Second, the proposed standards will resolve some doctrinal inconsistencies in the cases themselves, since not all of the Commission's or the judiciary's pronouncements go as far as the rules that would be overturned by this legislation.

Indeed, I must interject at this point, that I have sat through the entire session this morning and read some of the prepared statements. I have heard it stated that the current law of deception is clear and known to all. I have also heard it defined differently by different witnesses at this table. Indeed, the Commissioners themselves did not seem to agree on the basic controlling standards.

I, for one, am not surprised by this revelation. I think the committee has heard enough evidence this morning not only that the law of deception is less clear than some believe, but that it is torn by basic differences respecting policy conflicts that need to be resolved in this important field of regulation.

Perhaps most importantly, the standards that Chairman Miller has proposed reflect not only a careful balance between the central economic costs and benefits of regulating deception, but a sensitivity to the first amendment values that permeate any government attempt to regulate speech.

Recognition of these policies and values is not the exclusive province of the FTC or the courts. Both deserve and respect the serious attention of the Congress and this committee in particular as well.

Thank you, Mr. Chairman.

Senator **Kasten**. Mr. Collier, thank you very much.

As a former Chairman of the FTC, we particularly appreciate your help and your views. I may have some specific questions comparing the different kinds of proposals we have heard today.

But in a broader kind of a way, looking back over both the definition of unfairness and the definition and questions surrounding deception, you are aware of what this committee has put into the reauthorization bill on unfairness. I think you are also aware of the process we went through in order to try to reach a consensus, essentially as you suggested—codifying existing law and bringing groups together and moving forward.

Am I being overly optimistic in hoping that with a certain amount of work and more analysis such as we have gone through this morning that we could reach the same kind of consensus on deception? Here I guess we would be defining or I guess I should say codifying existing practice rather than codifying existing law, if we want to be technical.

Do you think we could go through the same kind of an effort and arrive essentially at an agreed to consensus on deception as we have been able to over the last few years on unfairness?

Mr. **Collier**. I think there are great prospects for that. I was very interested in Commissioner David Clanton's suggestion that the Commission might turn its attention to perparing for the committee a statement similar to the type they did in the unfairness field, stating its views on what the law of deception requires.

I think that would be a very productive piece of information for this committee, regardless of whether it decided to legislate or not.

I would make one other point in general on the legislation in response to much of what has been said this morning. There inevitably is going to be a lot of judgment at the Commission in deciding what is deceptive. The committee has to keep in mind—I think Commissioner Clanton made this point nicely this morning as well—that the wisdom of Commission action is not going to be guaranteed by any particular definition of deception. The Commission ultimately is going to make some determinations about the public interest in the allocation of its resources. There are many ways of supervising that by the Congress.

So I think that this is a very promising suggestion by Commissioner Clanton, and whether the committee acts immediately on the legislation or not, it would be appropriate for the Commission to do what Commissioner Clanton suggested it might be able to do.

[The statement follows:]

STATEMENT OF CALVIN J. COLLIER

It is a pleasure and a privilege to be here today to share with the Committee my views on proposals to amend the Federal Trade Commission Act by establishing legislative standards for the term "deceptive." I am here today in my own individual capacity and, although I represent clients who are interested in this subject, the opinions that I shall offer are not necessarily those of any other person or organization.

I would like to begin by applauding the Committee on its decision to conduct these hearings. The particular statutory phrase that you are considering today is worthy of your attention for several reasons. First and foremost, of course, is the fact that Section 5 of the FTC Act has served and should continue to serve as a key safeguard to protect consumers against dishonest business practices. This fundamental protection is supported not only by consumers but also by the overwhelming majority of businesses.

Second, broad hearings on the agency's deceptive practices jurisdiction is overdue. To my knowledge no similar inquiry has been held by Congress since that language was added to the FTC Act some 44 years ago. During that period, the Commission and the courts have erected a massive interpretive edifice upon the word "deceptive" and it is time that the Congress reviewed in depth what has been done by the other branches of government with its handiwork.

Third, these hearings are particularly appropriate in the wake of the deep concerns in Congress during recent years with the FTC's overall agenda and the scope of its powers. The action of the Committee on May 28, 1982, to report reauthorization legislation changing the Commission's basic mandates to regulate unfair practices and unfair advertising makes this inquiry particularly timely since the concepts of unfairness and deception are inseparably linked.

In order to evaluate the merits of legislation to define deception, one must begin with an understanding of the meaning of that term under current law. To date, this meaning has been provided primarily by the courts and the Commission itself.[1] The legislative history of the Wheeler-Lea Act, which imported the terms "unfair or deceptive" into Section 5, contains scant guidance from Congress regarding the intended meaning of deception.[2]

According to the Committee reports on the 1938 legislation, the phrase "unfair or deceptive" was added to Section 5 in order to deal with the Supreme Court's 1931 decision in *Federal Trade Commission* v. *Raladam Co.*, 283 U.S. 643. Although the Commission had been successfully challenging unfair and deceptive practices as "unfair methods of competition" since its creation in 1914,[3] the *Raladam* decision

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[1] Some special statutes expressly declare certain practices to be unfair or deceptive within the meaning of Section 5 of the FTC Act. This approach appears to be less of a Congressional attempt to actually spell out the meaning of these terms than a convenient means of invoking the powers of the Commission to enforce the particular requirements of those statutes.

[2] This judgment is corroborated by the fact that neither the Commission nor the courts have been able to point to authoritative and relevant legislative materials to support the interpretations described hereafter.

[3] E.g., *Royal Baking Powder Co.* v. *Federal Trade Commission*, 281 F.2d 744 (2d Cir. 1922): *Guarantee Veterinary Co.* v. *Federal Trade Commission*, 285 F.2d 853 (2d Cir. 1922); *Federal*

Continued

suggested for the first time that a finding of violation also required proof that the offender injuried its competitors.[4] Believing that proof of injury to rivals was an irrational requirement if injury to consumers could be demonstrated, the Commission sought and obtained a legislative dispensation from mandatory proof of competitive injury.[5]

In pursuing its goal of overruling the *Raladam* decision, Congress did not expressly consider other important questions that lurk in the term, "deceptive." For example, logic and subsequent experience teach that a finding of deception will usually require answers to several questions. including:

What is the meaning or interpretation of the allegedly deceptive representation?

Was the representation, as interpreted, untrue?

What effect did the deception have on consumers? Congress clearly seems to have intended that this latter question would be relevant under Section 5 and that a showing of consumer injury could be required.[6]

Moreover, to answer the basic questions of interpretation and effect, it is necessary to posit an actual or hypothetical consumer who would infer the alleged meaning and act upon it to his or her detriment. This need arises because languages and other forms of communication are inherently imprecise and because consumers may have infinitely different reactions to sellers' representations.

Finally, all of these inquiries require determinations regarding the type and amount of evidence or other proof that the FTC in the first instance and the courts on review will demand to establish liability.

Although congress did not expressly identify these lurking issues or provide much guidance for their resolution in particular cases, the Commission and the courts soon began to construct a statutory gloss that addressed each of them and others. Under Commission and judicial rules, the concept of "deception" became an extremely broad grant of authority. For example, according to these interpretations:

Trade Commission v. *Balme,* 23 F.2d 615 (2d Cir. 1928); *Indiana Quartered Oak Co.* v. *Federal Trade Commission,* 26 F.2d 340 (2d Cir. 1928).

[4] By the time that the Wheeler-Lea Act was passed, the courts had already begun to recede from Raladam.

[5] While the explicity exclusive purpose of the 1938 Amendments was to overturn Raladam's requirement of competitive injury, other themes were sounded by the Committee. For example, consumer or public injury was a stated predicate for Commission action under the new standard just as it had probably been under the original statute. Moreover, some opponents of the legislation argued that a general prohibition was too vague and should be replaced with a "laundry list" of prohibited practices. The listing approach was rejected for essentially the same reasons that such an enumeration of forbidden acts was rejected in 1914 when Congress prohibited "unfair methods of competition." It was felt that no laundry list could anticipate the ingenuity of ill-intended businesses and that the Commission, armed with very limited remedial powers (at that time), needed to operate under a general mandate to keep pace with the changing character of dishonest business practices. See e.g., Statement of R. E. Freer, Member of the FTC, Hearings on S. 3744 (March 10, 1936).

Ironically, Congress was much more instructive in crafting special provisions in the 1938 Amendments to regulate the advertising of foods, drugs and cosmetics. Section 15 of the Act, adopted simultaneously with the undefined phrase "unfair or deceptive acts or practices" did define a "false advertisement" of these products to consist of "an advertisement, other than labeling, which is misleading in a material respect; and in determining whether any advertisement is misleading, there shall be taken into account (among other things) not only representations made or suggested by statement, word, design, device, sound, or any combination thereof, but also the extent to which the advertisement fails to reveal facts material in the light of such representations or material with respect to consequences which may result from the use of the commodity to which the advertisement relates under the conditions prescribed in said advertisement, or under such conditions as are customary or usual."

The definition of "false advertisement" contained in Section 15 includes several general limiting principles that have been discussed in connection with the term "deceptive." These include a "materiality" requirement and the desirability of interpreting advertising claims according to objective standards. Those restrictions on Commission powers to find that false advertisements of foods, drugs and cosmetics are unlawful are ironic because of the obviously greater propensity of such claims to cause consumer injury. The justification for including these limitations appears to have been the fact that the government's enforcement powers to regulate these advertisements were significantly enhanced. Since adoption of the Wheeler-Lea Act, of course, the Commission's powers to enforce the general prohibitions of Section 5 have also been enhanced.

[6] Senate Report No. 221 (75th Cong. 1st Sess.) noted with approval a portion of the Supreme Court's discussion in *Federal Trade Commission* v. *Klesner,* 280 U.S. 19, 27 (1929), which stated the need for proof that purchasers were actually deceived is "an essential element of the cause of action," (p. 2). House Report No. 1613 (75th cong. 1st Sess. explained that the amendment would "prevent [unfair or deceptive] acts or practices which injuriously affect the general public as well as those which are unfair to competitors," (p. 3).

The Commission itself has broad discretion to interpret the meanings of representations and may infer the existence of claims that were not expressly made: [7] reviewing courts will not substitute their interpretations unless the Commission's findings are clearly erroneous: [8]

The Commission's conclusion that a representation is untrue will not be reversed by the courts unless it is not supported by substantial evidence in the record taken as a whole: [9]

The Commission is not required to prove actual consumer injury but only to conclude in its own expert judgment that the deceptive representations have a tendency or capacity to cause injury; [10] moreover, the perceived injury need not be substantial; [11]

In determining whether an alleged representation has in fact been made, the Commission is expected to interpret the seller's claims through the eyes of "wayfaring men, though fools," the "incredulous" and persons of otherwise diminished capacity; [12]

In determining whether the claims have a tendency or capacity to cause perceived consumer injury, the Commission is expected to imagine their effects on the same subnormal population; [13]

In deciding whether consumers actually interpreted the alleged claims as the Commission asserts, the Commission may disregard objective survey evidence and rely upon its own presumed "expertise." [14]

The cumulative effect of these "rules" and others [15] provide a solid basis for the criticism that "deception," like "unfairness," is about anything that the Commission says it is. Literally applied, the law of deception would condemn most commercial speech that is normal, unobjectionable, and actually very helpful to the great majority of consumers.

Supporters of the current law argue that these rules defining deception are not literally applied and that the FTC generally exercises its discretionary judgment to challenge only those practices that involve injurious falsehoods based on reasonable interpretations of claims.[16] Indeed, the Commission's final actions generally meet this standard. The present Commissioners and others that I have been privileged to serve for and with are reasonable and practical people. It is not surprising to me then that specific examples of final agency actions actually these sweeping standards to innocuous advertising are rare.

Opponents of legislation go on to argue that the FTC's generally commendable past performance in wisely using its broad powers defeats the need for legislation. That is where I part company for several reasons.

First, the current law is more than a grant of authority for Commission action. It is in all respects a statement of the bounds of permissible conduct. To the extent that the law is more demanding than the Commission's enforcement of it, we have the classical problems associated with laws that are not fully and literally enforced.

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[7] *Standard Oil of California* v. *Federal Trade Commission*, 577 F.2d 653 (7th Cir. 1978); *Simeon Mangement Corp.* v. *Federal Trade Commission*, 579 F.2d 1137 (9th Cir. 1973).

[8] *Citizen's to Preserve Overton Park* v. *Volpe*, 401 U.S. 402, 416 (1971).

[9] Id. at 414 *Transworld Accounts, Inc.* v. *Federal Trade Commission*, 594 F.2d 212 (9th Cir. 1979); Administrative Procedure Act § 706, 5 U.S.C. § 706(2)(E).

[10] *Chrysler Corp.* v. *Federal Trade Commission*, 561 F.2d 357 (D.C. Cir. 1977).

[11] See, e.g., Block Drug Co., 90 F.T.C. 893 (1977).

[12] *Federal Trade Commission* v. *Standard Education Society*, 302 U.S. 112 (1937); *ITT Continental Baking Co.* v. *Federal Trade Commission*, F.2d 207 (2d Cir. 1976); 532 *Florsheim* v. *Weinberger*, 346 F. Supp. 950 (D.D.C. 1972). Some Commission decisions articulate a "reasonable person" standard. Cf. Kroger Co., —— F.T.C. ——, 3 CCH Trade Reg. Rptr. ¶ 21,877 (September 25, 1981).

[13] See, e.g., *ITT Continental Baking Co.* v. *Federal Trade Commission*, supra.

[14] Ford Motor co., 87 F.T.C. 756 (1976). But see Kroger Co., supra, at n. 11.

[15] E.g., The Commission may, after finding that an advertisement is deceptive, infer that the deceptive information would be a material factor is the consumer's purchasing decision. *Federal Trade Commission* v. *Colgate-Palmolive*, 380 U.S. 374, 391–2 (1965). Advertisements capable of being interpreted in a misleading way are construed against the advertiser. *Resort Rental Car System, Inc.* v. *Federal Trade Commission*, 518 F. 2d 967, 964 (9th Cir. 1975).

[16] See FTC "Deceptive and Unsubstantiated Claims Policy Protocol." The Protocol, adopted in 1975, was designed to instruct the Commission staff in the execution of its advertising enforcement responsibilities. It identifies relevant factual inquiries for ascertaining consumer injury caused by deceptive advertising including, among other things, the extent to which consumers inferred the false meaning, the extent to which consumers inferred the false meaning, the factual basis for presuming its falsity, the likelihood of detrimental consumer reliance, and the extent of total consumer injury. The Protocol was designed to focus the the staff's inquiry into the " public interest" factors that are relevant under the statute to the complaint issuance function as well as the legal requirements of section 5.

Respect for the law enforcement agency is diminished and businesses are encouraged to ignore its clear mandates. To avoid these problems, Congress should try to bring the literal requirements of the law into conformity with reasonable enforcement strategies.

Second, the divergence between the law's literal requirements and its more reasonable applications breeds uncertainty and confusion. Advertisers spend additional societal resources that could be better used elsewhere reading the tea leaves of shifting enforcement policies. During the debates that have occurred to date on deception legislation, some have asserted that this concern with clarifying and refining the controlling standards is misplaced because the law of deception is well-known. I respectfully submit that this assertion is untrue. I am confident that many businessmen have no idea that the rules I recited earlier are the controlling standards for truthful advertising. I am also confident that many are not informed about the judgmental factors that these rules assign to a majority of the Federal Trade Commissioners.

Third, the FTC's generally commendable restraint in applying the law of deception in its final judgments of lawfulness obscures another serious problem with the lack of basic deception standards. The Commission is not simply a handful of Presidential appointees and their senior staff; it consists of hundreds of lawyers and investigators who possess varying viewpoints. The extraordinary breadth of the term "deceptive," like the term "unfair," simply encourages the pursuit of practices at the investigational stage that are never ultimately approved by senior staff or the Commissioners. Some of those unproductive and expensive inquiries can also be avoided by clarification of the Commission's authority.

Finally, the task of defining vague terms such as "deceptive" is one that most properly and ultimately belongs to Congress. Expansive delegation of authority to agencies is sometimes necessary, especially at the threshhold of a regulatory venture when the subtle questions have not yet been identified. However, after more than 40 years of interpretive experience Congress is ideally situated to evaluate these issues, and provide fresh guidance to the agency and the courts.

Although the current prohibition against deception is extremely broad and Congressional review of prevailing standards is timely, the longevity of the existing statute also justifies a careful approach to its amendment. Beneficial changes in existing law should meet several criteria.

First, they should not lead to unduly complicated proceedings or to unnecessary controversies about sufficiencies of evidence.

Second, they should not invite the courts to second-guess Commission judgments so long as those judgments conform to the new standards.

Third, any amendments to the law of deception should continue to vest meaningful discretion in the agency to make difficult decisions in close cases.

Of the various proposals that have been made to alter the current statute, those offered by Chairman Miller best meet these criteria. In his April 1 statement to this Committee, the Chairman proposed a two part test of deception. Under the first part, a representation would be found to be deceptive if consumers, acting reasonably in the circumstances, inferred an untrue meaning from a representation and if these consumers were likely to rely upon the untrue claim to their detriment. Under the second part, deception would exist if, without regard to consumer effects, the seller knew or should have known that its representation was false.

In general, the Chairman's proposals would implement standards for deception that the Commission has tended to follow in practice.[17] At the same time, the proposed standards would reduce the incidence of wasteful preliminary investigations which are influenced by the literal application of the current ambiguous definition of "deception." In addition, the proposed amendments utilize flexible concepts that are well-known to the law and the courts and that, as a result, should occasion little or no disruption in the course of enforcement. The net effect of the proposed changes would be to delineate the permissible bounds of Commission regulation of advertisements, while preserving the flexibility necessary to efficient administrative action.

The effects of the proposed changes on prevailing doctrine are selective but important.

1. None of the changes would alter the primary responsibility of the Commission in its adjudicative capacity to interpret the meanings of challenged representations. This interpretive function is and would remain a mixed determination of fact and judgment and the FTC's role as the novo fact finder would not change. Moreover,

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[17] See generally note 16, supra.

under well-settled and clearly codified rules of law, courts would not be entitled to substitute their findings for those of the Commission.

2. Neither would any of the changes alter the Commission's or the courts' responsibilities to determine the truth or falsity of the representation.

3. By confirming the Commission's need to find a likelihood of detrimental consumer reliance on the challenged representation, the proposed changes would modify existing doctrine but not the Commission's existing policy.

The detrimental reliance or consumer injury requirement would be satisfied in those situations where a consumer has been induced by a misrepresentation to buy that which he would not otherwise have bought. The key inquiry in any assessment of consumer injury is whether the consumer would have made a different decision if the misleading claim had been true. If the misrepresentation is material to the consumer's purchasing decision, such injury could occur.

These concepts of materiality and detrimental reliance are familiar. They are used, for example, in securities regulation. The Supreme Court has held that for the purposes of Rule 14a-9 of the Securities and Exchange Commission, which forbids false and misleading representations in proxy situations, "[a]n omitted fact is material if there is substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote." [18]

A similar standard is contained in the Commission's "Deceptive and Unsubstantiated Claims Policy Protocol." [19] This statement lists a number of questions to be answered by the staff when enforcement action is under consideration. These questions include reasons for assuming that the representation affects purchase decisions, price of the product, total volume of purchases, and the value of the product in the absence of the quality it is misrepresented as having.

Codification of a consumer injury standard would simply and explicitly reassert Congress' original intention in connection with the 1938 amendments.[20] Subsequent judicial and Commission decisions have sapped this intended requirement of any effect.

Under the proposal, the likelihood of injury rather than injury itself would be a sufficient basis for liability. This standard is satisfied if detrimental reliance would probably occur.

In the ordinary case, these conditions of liability could be established by proof that the false representation concerned a product characteristic that was important to consumers. In other cases where the deception concerns peripheral characteristics, additional inquiry into the existence of actual or probable consumer injury would be apropriate.

Although the proposed injury requirement would alter existing doctrine in many situations, another one of the proposals would dispense with this requirement in appropriate cases. Under the Chairman's proposal, the likelihood of detrimental consumer reliance would not be necessary if it appeared that the seller knew or should have known that the challenged representation was untrue.[21]

This alternative avenue to deception liability presumes consumer injury in those cases where the seller's conduct will, by definition, create unreasonable risks of its occurrence. For example, if a seller knew its representations would be false and made them anyway, it would seem reasonable to assume that some injury resulted to consumers. Similarly, if sellers carelessly make false representations, the probability of injury to consumers from that conduct may warrant an inference that it is likely to occur.

The "should have known" standard is the familiar negligence standard of the common law.[22] An advertiser would be responsible to exercise due care for the truth of reasonable interpretations which might be drawn from his assertions. This standard will focus the attention of both the Commission and the advertiser on the natural consequences of, and inferences from, the claims that are being made.

Authority to infer injury simply on the basis of the seller's conduct is not without some potential for agency abuse. Ordinarily one would expect to find sufficient evidence of consumer injury under the proposed test of detrimental reliance on material misstatements. Indeed, the absence of some such likely effects in a given case may call into question the conclusion that the respondent acted carelessly.

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[18] *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438, 449 (1976).

[19] See n. 16, supra.

[20] See note 5, supra.

[21] contrary to some of the criticisms that have been heard, the proposed inquiry into the seller's knowledge and due care would not be necessary to liability, merely sufficient. The Commission would only be required to meet this test if it were unable to find some injury to reasonable consumers from the false representation.

[22] According to the Restatement of Torts, Second, § 12 "[t]he words 'should know' are used . . . to denote the fact that a person of reasonable prudence and intelligence . . . would ascertain the fact in question in the performance of his duty to another, or would govern his conduct upon the assumption that such fact exists."

Moreover, liability for carelessness without injury would usually call for relief that was tailored to the violation. Appropriate orders in these cases would usually be directed at reforming the respondent's conduct in the future and not attempting to redress hypothetical injuries that cannot be shown.

Ultimately, reasonable containment of a "should have known" standard will depend upon the common sense of Commissioners and the judicially unreviewable requirement that the agency only initiate enforcement proceedings in the public interest. On the other hand, a statutory admonition to businesses to exercise due care in their representations to consumers seems reasonable.

To satisfy the "should have known" standard, the Commission will not need to prove that an advertiser intended the misleading consequences of his advertisement, but only that he should have foreseen that a reasonable consumer would understand him to be making the misleading claim. The standard will require objective and common sense assessments of the meanings of advertisements. The Commission is familiar with the "should have known" standard: it is now used by the courts and the Commission to determine the liability of advertising agencies for false or misleading advertising.[23]

Some have suggested that deception liabiity should be premised on a finding of substantial consumer injury. I am not convinced that this quantitative requirement should become a part of the legal standard. Traditionally, the Commission considers questions of substantiality at the complaint issuance stage as part of its required "public interest" determination, and even before then, as part of its resource allocation judgments. For example, the "Deceptive and Unsubstantial Claims Policy Protocol" is designed to develop information that is relevant to these important considerations.

On the other hand, I am not convinced that an express substantiality requirement would improve the definition of deception. There may be cases where the adverse consequences of an individual respondent's behavior is not substantial but where Commission action would be warranted to guard against its infectious influence on the behavior of others. Neither do I see the advantages of subjecting the issue of substantiality in this context to the rigors of the adjudicative process. Rather, judgments about the quantum of the Commission's beneficial contributions to consumer welfare should be assessed by Congress and the President through the appropriations, appointments and general oversight processes.

4. I am frankly surprised at the controversy which has erupted over the proposal to measure the impressions made by challenged representations under a standard of reasonableness. Under existing doctrine, an advertiser violates the statute by making claims which reasonable consumers did not think were being made. Liability arises for fanciful interpretations of advertising claims which would only be believed by "the ignorant, the unthinking, and the credulous." I cannot see any merit to retaining this caricature of a legal standard. Advertisers do not try to live up to it and the Commission rarely attempts to enforce it. It was crafted by the courts to save Commission decisions that were not worth saving; a clear case of bad cases making bad law which, in turn, makes more bad cases.[24]

The consumer-acting-reasonably-in-the-circumstances standard also will preserve liability for claims that mislead less than normal target audiences such as children. If an advertiser targets such a group, the standard would require consideration of how a reasonable member of it would interpret the claims and behave in response to it.

The current legal standard unduly suppresses truthful speech. By prohibiting claims that may mislead a small minority, the rule deprives the great majority of access to information that would be helpful and true. Restricting claims to those that are impervious to foolish interpretations restricts the flow of information and raises the costs of that which is ultimately provided. Clearly, the foolish man test of current law is a case of overregulation.

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[23] *Standard Oil of California* v. *Federal Trade Commission*, 577 F.2d 653, 660 (9th Cir. 1979); *Doherty, Clifford, Steers & Shenfield* v. *Federal Trade Commission*, 392 F.2d 921, 928 (6th Cir. 1968); see also *Carter Products, Inc.* v. *Federal Trade Commission*, 323 F.2d 523, 534 (5th Cir. 1963). The existing knowledge or negligence requirements that are applied to advertising agencies answers those who erroneously contend that the standards are alien to deception regulation.

[24] For example, the Commission found that consumers might interpret a skin moisturizer with the name "Rejuvenescense Cream" as implying that product would restore the appearance of youth, in *Charles of the Ritz Distributors Corp.* v. *Federal Trade Commission*, 143 F.2d 676 (2d Cir. 1944), and that consumers might interpret advertising of a "permanent" hair-coloring product as promising that it would color hair that had not yet grownn in *Gelb* v. *Federal Trade Commission*, 44 F.2d 580 (2d Cir. 1944).

Aside from Commission non-compliance with the current law, the major defense that has been offered for preserving these sweeping judicial interpretations of Section 5 is the protection it provides against exuberant judicial review. The foolish man test undoubtedly discourages courts from substituting their judgments for the Commission's. However, the proper relationship between the agency and the courts can be preserved without perpetrating standardless criteria of liability. Indeed, the Administrative Procedures Act which, post-dates the adoption of this substantive doctrine, does just that. In light of these well-established standards of judicial review, the foolish man standard for deception liability long ago outlived any claim it could make for legitimacy.

5. Finally, the effects of the proposed changes in legal standards on the types of evidence necessary to establish a violation will be modest, but in appropriate cases, important.

The standard of proof necessary to show injury or detrimental reliance will depend on the facts of each case, just as liability does under the current court-made rules. In some instances, the likelihood of detrimental reliance would follow from the nature of the representation itself. For example, if a false claim concerns a product feature which is important to consumers, injury can be inferred. In cases where the materiality of the misrepresentation is less obvious, some showing of probable injury may be necessary. If the Commission is able to show the materiality of the claim, no elaborate proof will be necessary. An advertister would not be foreclosed, of course, from presenting proof to rebut a disputable inference of injury.

The reasonable person standard is also one which is easily understood and applied by both the Commission and the courts. The common law of both tort and contract,[25] as well as the areas of securities regulation [26] and OSHA regulation,[27] for example, all employ reasonable man standards. The standard is an objective one, which does not require proof that any particular person did in fact act in a particular way. There would be no need to introduce into evidence elaborate statistical or psychological evidence about the beliefs of actual consumers. The Commission would retain discretion as the fact-finder to interpret advertisements without consumer testimony and to apply its informed judgment of how a normally intelligent target of the claims would understand the advertisement in question.

At the same time, respondents could (as they are permitted to do now) submit reliable evidence to show that consumers in fact did not infer the alleged meanings or regard tham as material. However, unlike the situation under current law,[28] the Commission could not disregard such proof, except at its peril.

Several additional issues have been publicly discussed in connection with possible legislative changes to the current law of deception. I would like to discuss a few of them.

The first issue concerns the effects, if any, on the Commission's doctrine of advertising substantiation. That doctrine, in a nutshell, provides that an advertiser must have a "reasonable basis" for his claims at the time he makes them. The Commission and the courts have been somewhat non-committal about whether this doctrine is grounded on the prohibitions of unfairness, deception, or some of both.

I have thought that the substantiation doctrine is best viewed as a corollary to the rule against deception and this view seems to be consistent with the agency's approach.[29] In applying the doctrine, the FTC has begun by interpreting claims, a step that also commences deception analysis. In practice, the next analytical step is to determine whether the alleged claim is the sort to which substantiation requirements will attach. In general, these have been performance claims that are objectively demonstrable. Finally, the Commission decides whether the substantiating material provides a sufficient "reasonable basis" for the claim.

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[25] See, e.g., Restatement of Torts, Second § 11.

[26] A "reasonably prudent investor" standard is applied in Rule 10b-5 cases. See, e.g., *City National Bank of Fort Smith, Ark.* v. *Vanderboom*, 422 F. 2d 221 (8th Cir. 1970).

[27] The Occupational Safety & Health Review Commission must demonstrate that a reasonable employer in the circumstances would have provided a particular sort of employee protection in order to support a finding of a violation of OSHA regulations. *Power Plant Div.* v. *Occupational Safety and Health Review Commission*, 590 F. 2d 1363 (5th Cir. 1979).

[28] Ford Motor Co., 87 F.T.C. 756 (1976). But see Kroger Co., supra, n. 12.

[29] Porter & Dietsch, 90 F.T.C. 866 (1977), modified on other grounds, 605 F. 2d 294 (7th Cir. 1979), cert. denied, 445 U.S. 950 (1980); National Dynamics Corp., 82 F.T.C. 488, 549–50 (1973), aff'd, 492 F. 2d 1333 (2d Cir.), cert. denied, 419 U.S. 993 (1974).

Analyzed from the standpoint of deception, the Commission's substantiation analysis involves two generally reasonable presumptions. First, that performance claims invite consumers to make an inference that the advertiser possesses a reasonable basis for them Second that consumers generally rely upon this inference in making product choices. For the most part, the Commission has invoked the substantiation doctrine only when these inferences have been reasonable.

Moreover, the potential excesses of the advertising substantiation doctrine are the same as those that accompany the deception concept and would also be reduced by the proposed legislation. Thus, the proposed requirement for interpreting claims as consumers acting reasonably in the circumstances would do would preclude far-fetched "implied" meanings which advertisers could not reasonably have known they were making and therefore could not have anticipated would require contemporaneous substantiation. The proposed requirements of materiality and detrimental reliance serve to bolster the twin substantiation requirements of objectively demonstrable performance claims and "reasonable" bases for making them.

The "know or should have known" alternative to establishing deception will also confirm the requirement of substantiation in many situations. For example, when an advertiser should have known that consumers would infer an objectively demonstrable claim and that a reasonable basis existed for making it, liability would result unless there is substantiation.

In short, the proposed changes to the deception standard are consistent with and supportive of the advertising substantiation doctrine as the Commission has generally applied it.

A second issue concerns the possible effects of the proposed changes on the theory that deception may be found where an advertiser has failed to disclose true but disparaging facts.

It is clear that this form of deception would continue to be reachable under the Chairman's proposals in appropriate cases. Indeed, a major example of the excessive breadth of current law is its application to misleading non-disclosures. The Commission's open-ended authority to discover after the fact that an advertiser should have but did cover after the fact that an advertiser should have but did not disclose some material fact is obviously subject to great abuse. Some consumers might want all sorts of undisclosed information and it can be highly unfair to single out a particular advertiser and some bit of information for non-disclosure liability.[30] Historically, the Commission has generally attempted to deal with this problem in two ways: first, by tartgeting its enforcement on sellers of products of dubious "social" merit who attract little sympathy and, second and more recently, by proposing Trade Regulation Rules which have prospective and industry-wide disclosure obligations.[31] The proposed changes to the deception standard will help to confine non-disclosure liability to reasonable bounds but it will not eliminate the serious potential for arbitrary use of this species of deception in all future cases.

The obligation to disclose is usually found to arise where a representation (express or inferred) is untrue unless it is accompanied by other representations or qualifications.[32] Under prevailing doctrine this obligation might be triggered by claims that unreasonable consumers infer and have the tendency or capacity to rely upon.[33] The proposal would assume that the disclosure obligation arises when consumers, acting reasonably in the circumstances, believe that the withheld facts were untrue, and, of course, would probably have acted differently if they had known the truth.

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[30] There are numerous, valid reasons why "material" information is not always disclosed in advertisements. First, of course, is the fact that consumers may not be willing to pay for its production and publication even though some of them may profess in opinion surveys to want it very much. Second, some material information is equally relevant to products other than the advertiser's own, causing the advertiser to be reluctant to give competing sellers a free ride on his production and publication costs. Third, some material information is very difficult and costly to produce in a non-deceptive form. Finally, of course, advertisers are unlikely to disclose information that reduces demand for their products. Ordinarily, we rely on competition to address the last problem.

[31] In my view, the Trade Regulation Rule procedure is generally superior to case-by-case adjudication as a means of imposing affirmative disclosure obligations both because it is fairer to sellers and because it requires the FTC to examine systematically the net benefits of the particular disclosure obligations being proposed. The latter advantage in a case-by-case context can and should be achieved by relying on the "uniform" standard rather than deception.

[32] Porter & Dietsch, supra, 90 F.T.C. at 865.

[33] *Compare Alberty* v. *Federal Trade Commission,* 182 F.2d 36 (1949), cert. denied, 340 U.S. 818 (1950) (deceptive non-disclosure occurs is "failure to reveal facts made important or of some consequence, because of other things claimed" or "because of the consequences from the use of the product.")

Once again, the Commission does not ordinarily press the legal doctrine to its limits. For example, in its so-called product defect cases, the Commission seems to be currently taking the postiion that a seller has an affirmative obligation to disclose serious defects that present unreasonable risks of economic harm or personal injury that are known to the seller and that are not apparent to consumers.[34] This theory would certainly be consistent with the modified concept of deception proposed by Chairman Miller.[35]

Although I am confident that these changes would be workable and beneficial, I could not quantify their postive contributions to the regulatory system. Here as in so many other areas where legislation establishes general rules for private sector conduct, evaluation of alternatives must proceed on the basis of close analysis and informed judgment.

From the standpoint of consumers and businesses alike, however, the proposed rules seem to be clearly superior to the court-made rules thay are designed to replace. A requirement that the allegedly deceptive claim be "material" seems superior to a rule that prohibits "immaterial" deception. Requirements of "detrimental reliance" and "reasonableness" seem equally superior to their antithese.

In addition to the common-sense advantages of these proposed standards, there are strong policies grounded in the First Amendment for adopting many of them. It must be remembered that the law of deception as developed by the FTC and the courts was designed entirely at a time when it was generally thought that commercial speech enjoyed no First Amendment protection.

In the landmark case of Virginia Pharmacy Board,[36] however, the Supreme Court exploded that assumption and in numerous subsequent cases[37] the court has reaffirmed the protected character of advertising. Although the court has concluded that deceptive commercial speech may be regulated, it has also recognized the crucial importance to consumers of the free flow of truthful advertising. Appreciation for this virtue of advertising is not apparent in the decisions under the FTC that have the word "deceptive" its expansive content.

Many of these past interpretations, in an avowed effort to protect a few consumers from possible harmful exposure to misleading claims, reprive the majority of consumers from information that is helpful. These rules also cause advertisers to incur additional costs not only to search for the law's meaning but to search for means of communication that are invulnerable to its prohibitions. These regulatory costs, like taxes, inevitably reduce the quantity of useful information made available to consumers.

By noting that regulation of deception imposes costs on society in the form of less truthful information I do not mean to suggest that there are no countervailing benefits. There certainly are. But wise rules governing deception should take both sides of the equation into account. Unfortunately, the current rules exaggerate the benefits and ignore the costs of controlling legislation.

Although the courts have not relied upon formal cost-benefit models in explicating the First Amendment, their interpretive rules are solidly grounded in the realization that imperfect regulation of harmful speech can and does suppress helpful speech.

As the court explained in Central Hudson Gas, supra: "If the communication is neither misleading nor related to unlawful activity, the government's power is more circumscribed. The State must assert a substantial interest to be achieved by restrictions on commercial speech. Moreover, the regulatory technique must be in proportion to that interest. The limitation on expression must be designed carefully to achieve the State's goal. Compliance with this requirement may be measured by two criteria. First, the restriction must directly advance the state interest involved; the regulation may not be sustained if it provides only ineffective or remote support for the government's purpose. Second, if the governmental interest could be served as well by a more limited restriction on commercial speech, the excessive restrictions cannot survive." 447 U.S. at 564.

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[34] See, e.g., American Motors Corp., Docket No. C-3093 (F.T.C. July 6, 1982) (complaint and consent order). Earlier cases appear to declare somewhat looser standards of liability.

[35] Significantly, liability under the rubric of deception for failure to disclose material facts is best known in the field of securities regulation where the standards being proposed for inclusion under Section 5 are already firmly ensconced by agency and judicial precedent.

[36] *Virginia State Board of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748 (1976).

[37] See, e.g., *Central Hudson Gas* v. *Public Service Commission*, 447 U.S. 557 (1980); *Linmark Associates, Inc.* v. *Township of Willingboro*, 431 U.S. 85 (1977); *Bates* v. *State Bar of Arizona*, 433 U.S. 350 (1977).

Both as a matter of sound regulatory policy and as a matter of enlightened constitutional principle, Chairman Miller's modest proposals for amending the FTC Act deserve your warm support.

Senator **Kasten**. Mr. Collier, thank you, and we will have some additional questions on some of the details.

I would like to thank all of the witnesses for their testimony today. The record will remain open so that members of the committee may submit written questions; and it is hoped that the answers for those questions would be back to the committee within roughly 2 weeks.

Thank you all again, and thank you particularly for your patience. Cal, we particularly appreciate your patience.

The hearing is adjourned.

[Whereupon, at 12:58 p.m., the hearing was adjourned, subject to the call of the Chair.]

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

NATIONAL CONSUMER LAW CENTER, INC.,
Washington, D.C., July 29, 1982.

CONSUMER SUBCOMMITTEE,
Russell Senate Office Building,
Washington, D.C.

DEAR SENATOR KASTEN: The National Consumer Law Center [1] appreciates this opportunity to provide the view of our low-income consumer clients regarding the proposal of FTC Chairman Miller to amend the FTC Act to limit the FTC's authority over deceptive acts and practices. We believe Chairman Miller's proposal is ill-advised, would be extremely costly to consumers and industry, and would be ineffective to deal with future problems of poor case selection by the Commission. Chairman Miller's proposal as explained by the March 25, 1982 memorandum of Timothy Muris departs from the decades old mission of the FTC to promote honesty in the marketplace. By carving out new exceptions to the doctrine of deception, the proposal will promote methods of dealing in which dishonesty will be lawful and will so increase the cost of prosecuting FTC cases within the remaining areas of unlawful conduct that the FTC's reduced enforcement resources will become even less of a deterrent to deceptive practices than they are now. If enacted the resulting unnecessary costs of Miller's proposal to consumers and honest businesses, and the resulting credibility loss of the mass marketing media will be debilitating and destructive to consumer confidence and the American economy. We believe that these effects would linger years after a repeal by the Congress which will realize the error of the proposal.

We agree that the problem of poor case selection by the FTC is one which should be addressed by your Committee. However, we disagree with the characterization and dimension of the problem described in the Muris memorandum and strongly disagree with the substance and approach of Chairman Miller's proposal to deal with the problem.

The solution to the problem is wise selection of Commissioners, a well-defined, clear statement of the FTC's internal enforcement priorities, careful management of the FTC resources to insure that they are devoted to those priorities, and Congressional oversight of those FTC decisions. This solution is not novel. It has been embraced by each of the FTC Chairmen over the last decade—Casper Weinberger, Miles Kirpatrick, Lewis Engman, Michael Pertschuk—this committee and consumer groups.

That the critics of the FTC—whether they be from Congress, business, consumer groups or an economics background—point to only a handful of poorly selected FTC cases over the last four decades proves that this approach works. That each group points to different cases illustrates the difference in their views of proper FTC priorities, but certainly not any deficiency in the well-developed FTC law of deception.

If the committee does decide to pursue further the course of changing the FTC law of deception by statutory amendment, NCLC recommends that it first subject the proposal to a careful analysis of its costs and benefits to consumers and business. NCLC is convinced that a change along the lines of Chairman Miller's proposal will cost far, far more than it saves. To suggest some costs of the proposal:

1. Consumers who commit the sin of trusting what they are told by sellers will no longer be protected by FTC law (unless the cynics are also misled) and will be fair game for unscrupulous operators. They will spend millions, if not billions, of dollars on unwanted or misrepresented products and services. This is a cost that must be estimated. Until it is clarified whether this group is intended to be 5 percent or 49

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[1] The National Consumer Law Center, Inc. is a non-profit corporation dedicated to serving the interests of low-income consumers across the country. The Center began in 1969 when Boston College Law School received funds from the Office of Economic Opportunity (OEO) to start a national support center concentrating on the legal problems of low-income consumers.

percent of the population by Chairman Miller's proposal, it will be difficult to estimate. Surely, the proponents of the proposal have some range in mind.

2. Consumers as taxpayers will have to pay more for FTC enforcement (or get less enforcement) because the FTC will have to contract for expensive surveys of consumers, prepare multitudes of witnesses, hire expert consultants and witnesses to present what are now routine prosecutions for deceptive acts and practices. Consumers as consumers will be paying through price increases in the goods they purchase as corporations pass on the costs for the preparation of the same type of evidence which they will develop as respondents in FTC proceedings. Lawyering costs will increase in these cases both for preparation and defense of the case and for the increase in appeals that will result from the proposed vague standards.

3. Delays in FTC enforcement will be increased by the uncertainly of the new law and the burgeoning litigation which will naturally result from the vagueness of the standards in Chairman Miller's proposal. Delays will increase the time during which even reasonably cynical consumers are subjected to deceptive acts and practices, increasing their expenditures on misrepresented products and services.

4. As the public learns that controversial opinions can be stated as if they were the truth, that "puffing" is lawful (the more incredible an advertiser's dishonesty the more lawful it will be), and that the public must not believe what it hears or reads unless most others would believe it, the credence given advertising and sales presentations will decline. This will result in new and expensive advertising campaigns to enchance seller credibility to win consumer purchases. The costs of these new marketing strategies will be ultimately passed onto consumers. Other advertisers will take the low road of hiring lawyers, market researchers, and advertising agnecies to exploit the new, ill-defined margins of lawful deception. These costs will also be passed along.

The failure of Chairman Miller or Mr. Muris to foresee, study and estimate such costs before trying out their proposal raises a serious inconsistency and imbalance in their approach to trade regulation. This committee should require them to provide a cost-benefit study of their proposal that is both serious and thorough.

Little would be gained in restating the criticisms which others amply presented in your March hearings. As stated by the National Association of Attorneys General and individual attorneys general, Chairman Miller's proposal will hamper state efforts to combat fraud and deception in the marketplace. The illusory nature of the quest for a definition of the "reasonable consumer" when consumer decisions are often in response to extra-rational appeals was then described by Professor Thain. Mr. Silbergeld's testimony repeatedly showed that most of the FTC cases relied upon to support Chairman Miller's assertion of past poor case selection by the FTC were cases which clearly deserved FTC attention when the entire case or its ramifications was examined.

Several additional points need to be made regarding the Muris memorandum's reliance on common law fraud principles. First, the elements of common law fraud borrowed in that memorandum—justifiable reliance, intent to deceive, the "puffing" and opinion defenses—were subject at common law to numerous exceptions that are not included in the Muris proposal. See, W. Prosser, Law of Torts §§ 107–109 (4th ed. 1971). As Professor Prosser notes in his treatise, the exceptions to the generally stated elements of fraud are as important as the general element. Those exceptions must be included in any substantive change to the FTC Act that is adopted. Second, as Professor Prosser also notes, the common law notion of fraud is based upon nineteenth century notions that buyers and sellers are adversaries on equal footing in their dealings. Those notions of strong individualism may have been appropriate in the nineteenth century when marketing techniques were face to face and less subtle, and products were less complex. It may have been appropriate when dealing with the sale of horses, wagons, and elixers when questions of medicine and physics were more questions of art than science. However, those notions are no longer valid now that products are so complex and beyond the understanding of most sophisticated consumers. The common law of fraud was abandoned in the FTC Act and state "little FTC" acts for precisely these reasons of mass marketing and technological change. The Miller proposal does nothing to show why these notions in their most facile form should be resurrected in this century. The answer to the problem of poor case selection by the FTC lies elsewhere; not in a change in the FTC Act standard of deception which has evolved from forty years of judicial interpretation into a predictable and just standard to promote honest dealings between merchants and consumers.

Very truly yours,

ROBERT J. HOBBS,
THOMAS MOORE,
Staff Attorneys.

ACTION FOR CHILDREN'S TELEVISION,
Newtonville, Mass., July 15, 1982.

Hon. BOB PACKWOOD,
Chairman, Committee on Commerce, Science, and Transportation,
Washington, D.C.

DEAR SENATOR PACKWOOD: It is our understanding that the Committee on Commerce, Science, and Transportation will soon be holding hearings on the "deception" standard in Section 5 of the Federal Trade Commission Act, which prohibits "unfair and deceptive acts or practices in or affecting commerce."

As you know, ACT is a national advocacy organization working to promote diversity in children's television programming and to eliminate deceptive and unfair television advertising directed to children. In a statement submitted to your committee in April 1982, I outlined ACT's position that Section 5 is vitally important to the integrity of Congressional policy, to the widely supported principle of consumer protection, to the promotion of fair marketplace competition, and to the nation's more than 40 million children.

Proposals to repeal or amend the FTC's standard of "deception" raise significant problems in the area of television advertising directed to children. The following points may provide a basis for some discussion during the hearings on "deception":

1. The prohibition against deceptive trade practices clearly protects children. Television advertising is the primary vehicle for reaching and persuading children to "participate" in the marketplace. Because the deception standard applies to television advertising directed to children and because children place indiscriminate trust in television commercials, retention of the deception standard is essential.

2. Both the courts and the FTC have used this standard to protect children from deceptive advertising. A series of decisions and orders has specifically prohibited certain advertising techniques that had the capacity or tendency to deceive children. The prohibitions have applied to TV commercials that exaggerated or misrepresented the performance of a product (Ideal, 1964; Mattel, 1971; Topper, 1971); that misrepresented that a food product would contribute to rapid growth (ITT Continental Baking Co., 1976); and that misrepresented that a collection of products sold separately was available as a set (Tomy, 1982).

3. Limiting the application of Section 5 only to "reasonable consumers" would eliminate children and other vulnerable groups. Whether an ad is deceptive may turn on the maturity of the target audience. Research shows that children's cognitive skills develop over time. Therefore, the notion of a "reasonable child," given these limitations, would not appear to be a legally viable concept.

4. In addition, it would be insufficient to subject only "factual claims" to a Section 5 allegation of deception. Television advertising directed to children rarely communicates factual information about price, size or durability; instead, techniques such as magical promises, animation, music, hero endorsements, authority-figure voice-overs, and promises of peer group acceptance are used to entice the child viewer. The very essence of children's television advertising is puffery: there are few, if any, factual claims to distinguish from opinion.

We very much appreciate your continuing interest in the need to protect children from unfair and deceptive advertising practices.

Sincerely yours,

PEGGY CHARREN, *President.*

UNIVERSITY OF WISCONSIN—MADISON,
Madison, Wis., August 2, 1982.

Senator ROBERT W. KASTEN, Jr.,
Russell Senate Office Building,
Washington, D.C.

DEAR SENATOR KASTEN: I have been following the hearings before the Senate Commerce Committee concerning proposals to limit the FTC's authority, with great interest. I appreciate the efforts of your office, especially those of Mr. Fullerton, in keeping your constituents apprised of the progress of these hearings. I earlier submitted a statement of my views as to the general thrust of these proposals at the time of the hearings held earlier this year. I adhere to those views, and I now make the following additional comments.

The proposals fall into three categories. One would eliminate FTC jurisdiction over the activities of licensed occupations, such as medical doctors, lawyers and dentists. A second would eliminate the agency's authority to attack unfair practices, or, in the alternative, provide a specific list of unfair practices which would be the only practices subject to attack by the agency as unfair. A third proposal would redefine the traditional definition of "deception" so as to narrow the agency's authority over such practices and, essentially, to conform it to the common-law standards for a private action for the tort of deceit.

I continue to believe that it would be a mistake that Congress would ultimately come to regret for any of these proposals to be adopted into law. I will comment on each proposal in order.

First, as to the limit of authority over the licensed occupations. I have engaged in issues of occupational licensing in Wisconsin both as an advocate and a scholar for the past six years. In addition, I have served on several committees involved in internal or state-supervised control of the licensed occupations, such as the State Bar Committee on Unauthorized Practice and, as a public member, the State Special Committee on Inter-Vision Care. None of my experience has led me to believe that removal of FTC authority over licensed occupations would be appropriate. I believe there is a significant and useful role for the states and the professions to play in regulation of these occupations but that, in the true meaning of federalism, the FTC needs to be available to cooperate with the states in matters which have national implications and to insure the existence of a national authority with jurisdiction beyond that of the specific anti-trust laws administered by the Department of Justice. Moreover, a continuing FTC presence in this field would make it less likely for the limited resources of state enforcement to be overwhelmed by the often huge resources available to the licensed occupations within the states. It is notable that the state attorneys general have not called for the FTC authority over the licensed occupations to be removed, indicating their belief that the federal presence of the FTC in this field is complimentary, rather than conflicting, with their own role of regulation. It is also telling, I believe, that the cry for such removal of FTC authority is limited, essentially, to one voice—that of members of the licensed occupations themselves, whose track record in self-regulation is considered highly suspect by virtually everyone outside those occupations. There is no reason to believe that members of the licensed occupations will act more in the broad public interest and less in their own economic self-interests, if they were to achieve their goal of a privileged status—immunity from FTC authority over their trade practices—than they did in the past. Indeed, there is every reason to believe the contrary.

As to the efforts to eliminate or restrict the FTC's authority over unfairness, I add the following observations to my earlier statement.

The definition of those practices which may be attacked as "unfair" even though not deceptive within the traditional legal use of that term and even though not violative of the letter or spirit of the anti-trust laws seems to focus mainly on two areas: one involves issues relating to health and safety and the other issues revolving around inappropriate or undue influence. Examples of the first area include depiction of dangerous acts as an incidental portion of television commercials and the distribution of inadequately packaged razor blades to consumers. Examples of the second are sales tactics which take advantage of a state of mind not in a position to deal with the workings of an idealized marketplace—such as the recently bereaved, or young children. Removal of such jurisdiction from the FTC in the name of "deregulation" seems dubious at best. Few respected observers of the economic process see much benefit in actions which would encourage reckless or unsafe conduct or allow unreigned preying on susceptable minds. As to the suggestion that "unfairness" be retained but limited to a specified list of unfair practices, the arguments successfully marshalled against this approach in 1914 when the initial version of the Federal Trade Commission Act was passed by Congress remain convincing today. Limiting unfair practices to a "laundry list" of specified misconduct not only invites the invention of conduct which will be immune from attack because it has been carefully structured so as to avoid falling within the letter of the Act although the conduct may clearly violate the spirit of the Act; such a limited definition of unfairness ignores technology and invocation, leaving the law in the position of playing a never-ending game of "catch-up" with business developments and practices not contemplated by the law because they were not envisioned by lawmakers when they were drafting their lists. There is obvious loss and little, if any gain, in tinkering with the present state of "unfairness" under section 5 of the Federal Trade Commission Act.

As to the definition of deception, it is my understanding that the Commission has been asked to study the manner in which it has defined deception over the years and to submit its report of that study, upon completion, to Congress. I believe this is a logical means of considering the issue raised by Chairman Miller and his staff, viz, is there any need to redefine, for purposes of section 5, the term "deception" so that it would follow more closely the more narrow common law definition of that term? I would suggest that it would also be appropriate for the Committee to receive a study of the interpretation of the term "deception" under common law standards for purposes of comparison, with strong attention given those misrepresentations not actionable under common law. I respectfully submit that it would be most appropriate for the Committee to take into account the issue of whether, as I believe, it is important for public law to set standards of conduct which are higher than those set by the courts for private controversies.

I would further suggest that the views of those state officials responsible for monitoring and attacking deception under the "little FTC Acts" of their states or their "Printers Ink" statutes and their counterparts be given heavy weight in reviewing the issue of the proper standard of deception. It is my impression that these officials, who are on the front firing lines of sharp practices, view the conduct of consumer transactions through less rosier-hued glasses than those worn by Chairman Miller and his staff.

I appreciate the opportunity to express my views on these important matters. I certainly hope that the result of careful consideration of the issues will be a determination to leave FTC authority over the licensed occupations, and the definitions of unfairness and deception, unchanged.[1]

Sincerely,

GERALD J. THAIN,
Professor of Law.

GENERAL FOODS CORP.,
White Plains, N.Y., August 5, 1982.

Hon. ROBERT W. KASTEN,
Chairman, Committee on Commerce, Science, and Transportation,
Washington, D.C.

DEAR SENATOR KASTEN: We very much appreciate the opportunity to include in the record of the hearing held by the subcommittee on July 22, 1982 the views of General Foods Corporation concerning the FTC's deception power.

General Foods Corporation is one of the nation's major manufacturers of food and beverage products. We are also one of the nation's leading advertisers. Speaking as such, we believe that it is in the public interest, as well as our own, that the consumer be able to rely on advertising claims to be truthful and not misleading or deceptive. In a marketplace as vast and complex as ours, the consumer's right to such advertising must be insured both by the rule of law and through the credibility of the ethical advertiser. Absent this, both the consumer and the ethical advertiser are at the mercy of the unethical and unscrupulous. We are convinced, therefore, that it is important to the proper working of our competitive system that the FTC be a viable and effective regulatory agency.

In this regard, we believe that the proposals concerning the "deception" power of the FTC advocated by the Chamber of Commerce of the United States, and by the American Advertising Federation, American Association of Advertising Agencies and The Association of National Advertisers go too far in attempting to redress and control what some may consider to be overly aggressive behavior on the part of the FTC.

Competitive pressures can be destructive as well as constructive. We have long favored the self-regulation of business and have taken an active role in founding and supporting the National Advertising Division of the Council of Better Business Bureaus. However, without the presence of an FTC with believable "deception" power, we are convinced that effective self-regulation of advertising would be difficult if not impossible. The "deception" proposals noted above would, we feel, materially weaken the FTC's power to prosecute deceptive advertising cases and would eliminate it entirely with regard to most grocery store consumer goods advertising.

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[1] I recognize that the Commerce Committee earlier this year voted to adopt the definition of unfairness embodied in the FTC's policy statement of December, 1980, concerning that topic. However, for the reasons stated herein, as well as those given in my March, 1982 statement, I believe that it would be unfortunate were that standard ultimately to be adopted into law, and, since the issues are closely connected to the definition of deception and remain before the Congress, I have addressed them here.

The natural consequence could be a downward spiral of truthfulness in advertising, eventually drawing all advertising to the lowest common denominator to the detriment of both consumers and advertisers.

There may well be room for improvement in certain of FTC's powers and methods of operation. An example is the ex cathedra power of the FTC to declare an advertisement deceptive, relying only on its own "expertise". It would seem, however, that many of the problems with the activities of the FTC stem from over zealous behavior. We are not at all certain that a legislated definition of "deception" is either necessary or will result in appropriate change in behavior. Forty years of judicial precedent should not be overthrown for, at best, a questionable benefit, and the certainty of creating a long period of legal uncertainty.

Changes in the FTC Act can have far-reaching and unintended consequences. We pledge to you and other interested legislators all possible assistance and cooperation in seeking solutions to such problems as may exist with the FTC. We suggest, however, great caution in proceeding in the "deception" definition matter.

Very truly yours,

ROBERT Y. FOX,
Associate General Counsel.

NRMA,
Washington, D.C., August 6, 1982.

Hon. ROBERT PACKWOOD,
Chairman, Committee on Commerce, Science, and Transportation,
Washington, D.C.

DEAR MR. CHAIRMAN: The National Retail Merchants Association ("NRMA") commends the Senate Committee on Commerce, Science and Transportation for its efforts in reviewing the scope of the Federal Trade Commission's authority to challenge practices as "unfair" or "deceptive." In its letter of April 7, 1982, to Senator Robert W. Kasten, Jr., NRMA expressed its hope that a studied review of the FTC's powers would result in the emergence of an improved and streamlined agency. In this letter, which NRMA requests become a part of your hearings on proposed amendments to the FTC Act, NRMA reiterates its concerns and, in particular, addresses the issue of the FTC's authority in the realm of "deception."

NRMA is a voluntary, non-profit trade association whose over 3,500 members operate more than 35,000 departments, chain and specialty stores throughout the nation. NRMA's members are subject to regulation by the FTC and are therefore directly interested in the scope of the agency's authority.

Although NRMA's April 7, 1982, letter focused primarily on the FTC's powers in the "unfairness" area, it also briefly discussed issues concerning "deception." In particular, NRMA suggested that Congress should instruct the FTC that the correct measure for determining whether an advertisement is deceptive is whether it is likely to mislead consumers acting reasonably under the circumstances. In that letter, NRMA also noted that the FTC has often relied on its naked "expertise" to interpret claims and, as a result, has at times construed advertisements as making claims that few, if any, reasonable consumers would derive from such advertising messages. Prohibiting advertising claims as deceptive on the basis of purely subjective interpretations not related to realistic consumer perception can have a chilling effect on the dissemination of true and useful information. Moreover, pursuing such unwise cases wastes the FTC's limited resources.

NRMA continues to believe that the scope of the FTC's authority to challenge practices as deceptive deserves further study in order to reduce the considerable uncertainty in current law. Greater certainty of the law would provide direction to those subject to the FTC's jurisdiction and would ensure meaningful judicial review of the FTC's actions.

In particular, consideration should be given to the nature and amount of support the FTC should have as basis for its interpretations of advertising messages. In this regard, the FTC should heed the practice of courts construing advertising under Section 43(a) of the Lanham Act 15 U.S.C. § 1125(a), which has been used by advertisers to challenge as deceptive claims made by competitors. In such cases, courts have generally distinguished between advertising claims that are "false on their face" and implied claims. Whereas the falsity of a "false on its face" claim is easily ascertained, the falsity of an implied claim depends on the manner in which it is perceived. Accordingly, before determining that an implied claim has the tendency to deceive consumers, courts have generally required evidence showing how consumers have interpreted the challenged claim, See, e.g., *Coca-Cola Co.* v. *Tropicana Prod-*

ucts, Inc. 538 F. Supp. 1091 (S.DN.Y. 1982); *American Brands, Inc.* v. *R.J. Reynolds Tobacco Co.,* 413 F. Supp. 1352 (S.D.N.Y. 1976). The FTC should similarly be required to have a real reason to believe that consumes interpret advertising claims in the way the FTC believes they do.

NRMA appreciates this opportunity to submit its views and hopes this Committee will agree with NRMA that the FTC's authority to prohibit deceptive practices should be thoroughly re-examined.

Sincerely,

VERRICK O. FRENCH,
Senior Vice President, Governmental Affairs.

STATE OF NEW YORK, DEPARTMENT OF LAW,
New York, N.Y., August 10, 1982.

Hon. ROBERT PACKWOOD,
Chairman, Committee on Commerce, Science, and Transportation,
Washington, D.C.

DEAR MR. CHAIRMAN: I am writing to express serious reservations concerning the proposed amendments to the Federal Trade Commission Act under consideration by your Committee.

I am pleased that the National Association of Attorneys General (NAAG) has submitted an extensively researched response to many of the proposed changes, and I fully endorse the NAAG submission. It adds a needed historical perspective on the amendments to section 5(a) suggested by Chairman Miller. Quite correctly, it points out that these proposals, if enacted, will produce a flood of litigation in every state and federal court, as litigants and judges struggle to forge understandable principles out of the new subjective standards.

I am particularly troubled by one aspect of the Chairman's proposals. This issue, given less emphasis than others in the NAAG submission, concerns part "b" of the following proposed language:

A deceptive act or practice is a material representation that (a) is likely to mislead consumers, acting reasonably in the circumstances, to their detriment, or (b) that the representer knew or should have known would be misleading.

Although the requirement that the representer "knew" that the representation would be misleading is only an alternate definition of a "deceptive" act, this proposal nevertheless grafts onto the FTC Act a scienter element implicitly rejected by congress and explicitly rejected by courts construing consumer legislation throughout this century. *FTC* v. *Algoma Lumber Co.,* 291 U.S. 67, 81 (1934). Until now, when I or other Attorneys General could not prove scienter, we would forego criminal penalties, but could at least pursue civil remedies. The proposed addition of scienter element to the FTC Act blurs this time-tested distinction.

Further, it is not clear whether the proposed definition of "deceptive act or practice" will call into question a principal's heretofore strict responsibility for his agent's representations, irrespective of the agent's real or apparent authority to make the representations, and whether or not the principal had knowledge of or discouraged the misrepresentations. *Parke, Austin & Lipscomb* v. *FTC,* 142 F.2d 437, 440 (2d Cir.), cert. denied, 323 U.S. 753 (1944). I firmly believe that strict responsibility would continue as the standard; however, if this amendment is enacted, this issue, and other foundations of consumer protection law, will be re-litigaed after decades of settled practice, thus squandering scarce law enforcement resources.

I urge that the Committee take these problems, as well as those raised n the NAAG submission, into consideraiton as it reviews the proposed amendments to the FTC Act.

Sincerely,

ROBERT ABRAMS.

GENERAL ELECTRIC CO.,
Washington, D.C., September 1, 1982.

Hon. ROBERT W. KASTEN, Jr.
Chairman, Committee on Commerce, Science, and Transportation, United States Senate, Washington, D.C.

DEAR SENATOR KASTEN: At the Consumer Subcommittee's recent hearing on the Federal Trade Commission's "deception" jurisdiction, the point was made—as it has been in the March 1982 FTC reauthorization hearings—that any change in Section 5 of the Federal Trade Commission Act would have an adverse effect on the consumer-protection activities of theose states which have modeled their laws on the FTC Act and follow FTC and federal court interpretations of the Act.

We have examined this proposition and have concluded that this is not a sound objection to amendment of the FTC Act. We enclose a memorandum summarizing our conclusions and respectfully request that it be included, with this letter, in the record of the July 22 proceeding.

Very truly yours,

MARTIN F. CONNOR.
ROBERT H. KLEIN, Jr.

Enclosure.

EFFECT OF AMENDMENT OF THE FTC ACT ON STATE CONSUMER PROTECTION LAWS

I. State Statutes Regulating Unfair or Deceptive Acts

(1) FORMS OF STATE STATUTES

Every state and the District of Columbia has enacted a statute of some kind to prevent unfair, deceptive or misleading business practices. Since 1966, the FTC has encouraged states to pass such legislation, and in 1967, as the result of discussions between the Commission and state officials, the model Unfair Trade Practices and Consumer Protection Act was drafted. See Schulman, Little FTC Act: The Neglected Alternative, 9 John Marshall J. 351, 352 (1975). The 1970 revision of the model act, upon which the majority of states have patterned their statutes, contains three alternate forms of coverage. See Unfair Trade Practices and Consumer Protection Law-Revision § 2, reprinted in Council of State Governments, 1970 Suggested State Legislation (Vol. XXIX).

Twenty-two state consumer-protection statutes follow the model act's first alternative and contain language either identical or similar to the broad proscription of Section 5 of the FTC Act, prohibiting "unfair methods of competition and unfair or deceptive acts or practices in trade or commerce." See Appendix, Column 1. In six other jurisdictions, the consumer-protection statute reaches unfair and deceptive acts or practices, with unfair methods of competition usually addressed in a separate statute. See Appendix, column 2.

The model act's second alternative prohibits false, misleading, or deceptive acts and practices. The consumer-protection statutes of sixteen states either follow or are similar to the model. See Appendix, columnn 3.

The third alternative prohibits certain itemized practices, with a catch-all phrase designed to reach other forms of unfair or deceptive acts. This alternative was derived from the Uniform Deceptive Trade Practices Act, promulgated by the National Conference of Commissioners on Uniform State Laws In 1964. See Unfair Trade Practices and Consumer Protection Law-Revision introductory note at 1, reprinted in Council of State Governments, 1970 Suggested State Legislation (Vol. XXIX). A total of thirty-two jurisdictions use such a listing approach in their consumer-protection statutes. See Appendix, column 4.

A small number of these states, however, have patterned their statutes not on the FTC model, but on the original Uniform Deceptive Trade Practices Act. As will be discussed more fully below, this distinction is important because the courts of at least three of these states look to the common law, rather than to decisions interpreting the FTC Act, to construe their statute.

"Unconscionable consumer sales practices" are prohibited, along with other itemized practices, in the Uniform Consumer Sales Practices Act, also promulgated by the National Conference of Commissioners on Uniform State Laws. *See* D. Rothschild and D. Carroll, Consumer Protection: Text and Materials § 8.04 (2d ed. 1977). That or some other form of unconscionability provision has been included in the consumer-protection statutes of fifteen jurisdictions. See Appendix, column 5.

Unlike the Federal Trade Commission Act, forty-three state statutes expressly provide that consumers may bring actions for damages against those engaged in prohibited practices. See Appendix, column 6. A number of these statutes provide for multiple damage recoveries, recision of transactions, and the recovery of attorney's fees. See U.S. Dept. of Justice, National Institute of Justice, Consumer Fraud at 22, 23 (1982). While the statutes of Arizona and Delaware do not expressly provide for private damage actions, this right is inferred by decisions of the Supreme Courts of those states. *Sellinger* v. *Freeway Mobile Home Sales, Inc.*, 110 Ariz. 573 P.2d 1119 (1974); *Young* v. *Joyce*, 351 A.2d (Del. Supr. 1975).

(2) RELATION OF STATE AND FEDERAL STATUTES

(a) Express statutory mandate

An important feature of the FTC's model act is its recommendation that state consumer-protection statutes contain some form of the following language: "unfair methods of competition and unfair or deceptive acts or practices are to be construed in light of decisions under the Federal Trade Commission Act." See Schulman, Little FTC Act: The Neglected Alternative, 9 John Marshall J. 351, 353 (1976). Currently twenty-four states incorporate some form of this language, or otherwise express its intention, in their consumer-protection statutes. See Appendix, column 8.

For example, the Massachusetts statute provides:

It it the intent of the legislature that in construing paragraph (a) of this section in actions brought under sections four, nine and eleven, the courts will be guided by the interpretations given by the Federal Trade Commission and the Federal Courts to section 5(a)(1) of the Federal Trade Commission Act (15 U.S.C. 45(a)(1) as from time to time amended. Mass. Gen. Laws Ann. ch. 93A, § 2 (b) (West Supp. 1981).

Other states have expressed this intention by saying that "due consideration and great weight" should be given to decisions construing the FTC Act, see, e.g. Fla. Stat. § 501.204; Md. Com. Law Ann. § 13–105, or that the statute should be construed to be "consistent" with interpretations of the FTC Act. See, e.g. Ga. Code § 106.1201(e); Tenn. Code Ann. § 47–18–115. The Washington statute, which prohibits unfair and deceptive acts or practices, states that its purpose is "to complement federal law" and that state courts in contruing the statute, should be "guided by the interpretations of federal courts of federal statutes dealing with the same material." Wash. Rev. Code § 19.86.920.

Thirty-five state consumer-protection statutes authorize the state enforcement agency to promulgate regulations interpreting the act. Seven of these statutes require regulations promulgated by the enforcement agency to be "not inconsistent" with federal interpretations of the FTC Act. See Appendix, column 7.

Numerous reported decisions by courts in states with consumer-protection statutes expressly referencing the FTC Act illustrate situations in which the courts have used FTC Act precedent in interpreting the state act. For example, in *Com.* v. *Decotis et al.*, 316 N.E.2d 748 (Mass. 1974), the Massachusetts Supreme Judicial Court utilized general principles of FTC cases to affirm a judgment that certain actions by a mobile home park operator violated the Massachusetts statute prohibiting unfair trade practices. In *Slaney* v. *Westwood Auto, Inc.*, 366 Mass. 688, 322 N.E.2d 768 (1975), the court stated that the FTC Act had been "wholly incorporated" into the Massachusetts consumer-protection statute. See also, *PMP Assoc., Inc.* v. *Globe Newspaper Co.*, 366 Mass. 593, 321 N.E.2d 915 (1975).

In *Lightfoot* v. *MacDonald*, 86 Wash. 2d 33, 544, P.2d 88 (1976), the Supreme Court of Washington held that certain acts of neglect by an attorney did not violate the Washington Consumer Protection Act, basing its decision on federal decisions interpreting the FTC Act. See also *Fisher* v. *World-Wide Trophy Outfitters, Ltd.*, 15 Wash. App. 742, 551 P.2d 1398 (Ct. App. 1976).

In *Christie* v. *Dalmig, Inc.*, 396 A.2d 1385 (Vt. 1979), the Vermont Supreme Court relied on the U.S. Supreme Court's definition of "unfairness" from *FTC* v. *Sperry & Hutchinson*, 405 U.S. 233 (1972) in finding a violation of the state statute. See also *Fitzgerald* v. *Chicago Title & Trust Co.*, 46 Ill. App. 3d 526, 361 N.E.2d 94 (App. 1977); *Spradling* v. *Williams*, 553 S.W.2d 143 (Tex. Cru. App. 1977); *State* v. *O'Neill Investigations, Inc.*, 609 P.2d 520 (Alaska 1980); *Island Tobacco Co., Ltd.* v. *R. J. Reynolds Tobacco Co.*, 627 P.2d 260 (Hawaii 1981).

Despite statutory mandates in these jurisdictions that state courts afford FTC Act interpretations "due consideration and great weight," or that the courts be "guided" by federal decisions, the overwhelming view of courts in these states is that FTC Act precedent is not binding on their decisions construing state consumer-protection statutes. For example, in *Island Tobacco Co., Ltd.* v. *R. J. Reynolds Tobacco Co.*, 627 P.2d 260 (Hawaii 1981), where the statute provided that courts "will be guided" by FTC Act decisions, the court stated that such precedent is "only a guide" and that federal law must be interpreted in light of and in accordance with conditions in the state. See also *State ex rel. Kidwell* v. *Master Distributing Co.*, 101 Idaho 447, 615 P.2d 115 (1980), stating that federal case law is not binding, but persuasive.

In *State* v. *Readers Digest Assoc. Inc.*, 81 Wash. 2d 259, 501 P.2d 290 (1972), the Washington Supreme Court stated that courts in the state may consider pertinent federal court interpretations, but in each case, the determination that a practice violates the state statute is for the state courts to decide. According to the court, an attempt by the legislature, in enacting the state statute, to adopt future federal rules, regulations or statutes would amount to an unconstitutional delegation of legislative power. Because it found federal interpretations under the state scheme to be guiding rather than binding, the court held that there had been no unconstitutional delegation of power. 81 Wash. 2d at 263, 501 P.2d at 294.

A different issue was presented in *Dept. of Legal Affairs* v. *Rogers,* 329 So. 2d 257 (Fla. 1976). In that case, the Florida Supreme Court held that the plaintiff, the executive agency assigned to enforce the state consumer-protection statute, was required to follow FTC Act precedent made before the enactment of the state act, in order to save the statute's constitutionality. The statute provided that "due consideration and great weight" should be given to decisions of the FTC and federal courts, and also required that the Department's rules be "not inconsistent" with rules of the Federal Trade Commission. If the statute were read to permit, but not require, the enforcement agency to follow FTC Act precedent made prior to the state statute's adoption, said the court, the act would fail as an impermissable delegation of legislative power because adequate standards of guidance would not have been given to the executive branch. 329 So. 2d at 265.

(b) No statutory mandate

Courts in the majority of states whose consumer protection statutes do not explicitly reference the FTC Act take into account nonetheless decisions construing Section 5 of that act when deciding cases under state consumer-protection statutes. It is a recognized principle of comity that when a state passes a statute which is modeled after a statute of another jurisdiction, whether federal or state, the courts of the state will be highly persuaded by the interpretations given by courts of the original jurisdiction to words contained in the statute. While the out-of-state decisions are not binding, courts in the state will often give the same interpretation to the statutory language as was given by the courts of the original jurisdiction before the act was adopted in the second state. See, e.g. *State* v. *Anderson,* 515 S.W.2d 534 (Mo. 1974); *No-Oil Inc.* v. *City of Los Angeles,* 118 Cal. Rptr. 34, 529 P.2d 66 (1974); *University of Oregon Co-op Store* v. *State Dept. of Revenue,* 542 P.2d 900 (Oreg. 1975).

Courts in states having consumer protection statutes with no direct reference to the FTC Act have used this principle in determining the effect of FTC Act precedent on actions arising under the state statutes. For example, in *Johnson* v. *Phoenix Mutual Life Ins. Co.,* 300 N.C. 247, 266 S.E.2d 614 (1980), the Supreme Court of North Carolina stated that because the language of the North Carolina statute prohibiting unfair and deceptive practices closely resembles the language of Section 5 of the FTC Act, and because that similarity is not accidental, it is appropriate to look to federal decisions interpreting Section 5 for guidance in construing the state statute. 266 S.E.2d at 620. See also *Comm. by Creamer* v. *Monumental Properties, Inc.,* 459 Pa. 450, 329 A.2d 812 (1974); *Guste* v. *Demars,* 350 So. 2d 123 (La. App. 1976); *State by Leftkowitz* v. *Colorado State Christian College of the Church of the Inner Power, Inc.,* 76 Misc. 2d 50, 346 N.Y.S.2d 482 (1973). In *Hardy* v. Toler, 288 N.C. 303, 218 S.E.2d 342 (1975), the North Carolina Supreme Court made clear that while decisions interpreting the FTC Act may offer some guidance, they are not controlling when state courts interpret the state consumer-protection statute. As is true in states whose statutes contain a direct reference to the FTC Act, this is the general view in states with statutes having no such reference. Mass. Gen. Law Ann. ch. 93A comment at 65 (West Supp. 1981); 2 Consumer Law Handbook 121 (1972).

(c) Relation to common law

As stated earlier, a small minority of states, with consumer protection statutes modeled after the Uniform Deceptive Trade Practices Act, do not look to FTC precedent to construe the state statute, but instead look to the common law. In *Young* v. *Joyce,* 351 A.2d 857 (Del. Supr. 1975), the Delaware Supreme Court held that the state's Deceptive Trade Practices Act, Del. Code Ann., tit. 6 §2531 et seq., having codified the UDTPA, which in turn had codified the common law, precluded the plaintiff from bringing a claim based on a practice not recognized as unfair at common law. See also *Schmidt Enterprises Inc.* v. *State,* 354 N.E.2d 247 (Ind. Ct. App. 1976) (stating that because the Indiana act had codified the common law, it was appropriate to look to decisions interpreting the common law of fraud in construing the statute).

The frequency with which state courts refuse to look beyond the common law in construing state consumer-protection statutes appears to be declining. The Uniform Deceptive Trade Practices Act has been criticized for its narrow approach and its ease of circumvention. See Note, Consumer Protection by the State Attorneys General: A Time for Renewal, 49 Notre Dame L. 410, 414 (1973); 2 Consumer Law Handbook 124 (1972). As discussed earlier, alternative three of the model act recommended by the FTC is similar to the UDTPA, but contains a provision designed to broaden the act's prohibitions and also provides that FTC Act precedent be used in interpreting it. See Unfair Trade Practices and Consumer Protection Law-Revision §§2, 3, reprinted in Council of State governments, 1970 Suggested State Legislation (Vol. XXIX).

A number of states which had first adopted consumer-protection statutes based on the UDTPA have also enacted statutes based on the FTC models, thus effectively proscribing conduct not prohibited by the UDTPA. See, e.g. Ill Rev. Stat. ch. 121 1/2 §§261, 311; Neb. Rev. Stat. §§59-1601, 87-302. *Compare National Football League Properties Inc.* v. *Consumer Enterprises Inc.* 26 Ill. App. 3d 814, 327 N.E.2d 242 (App. Ct. 1975) (holding that the Illinois Deceptive Practices Act, Ill. Rev. Stat. ch. 121 1/2 §§311 et. seq., merely codifies the common law) with *Fitzgerald* v. *Chicago Title & Trust Co.*, 46 IIL. App. 3d 526, 361 N.E.2d 94 (1977) (stating that it is proper to look to FTC Act precedent to construe the Illinois Consumer Fraud Act, Ill. Rev. Stat. ch. 121 1/2 §§261 et seq.)

II. The Effect of Amendment of the FTC Act on Enforcement of State Consumer Protection Statutes

(1) Differences between state and federal concerns, statutory goals and enforcement schemes have led state courts to rely only selectively on federal decisions interpreting the FTC Act, which reduces the effect of changes in such precedent on the states.

While state courts, in interpreting consumer-protection statutes, acknowledge a legislative intent that FTC Act decisons be used as guides in interpreting state acts, numerous cases illustrate that courts also recognize that circumstances at the state level make wholesale adoption of FTC Act precedent unwise. This realization has led state courts in many cases to give less weight to federal precedent where state purposes would be better served by interpretation of the state act which differs from federal interpretation of the federal act. As a result of this selective reliance on federal decisions construing the FTC Act, amendment of the Act would have less effect on enforcement of state consumer-protection statutes than might otherwise seem to be the case.

A number of courts have focused on the difference in enforcement schemes between state statutes and the FTC Act and have concluded that following federal precedent in certain instances might defeat the purpose of a state act. As discussed earlier, forty-five states allow individuals to bring private actions against persons violating state consumer-protection statutes, and this is one respect in which courts have found it necessary to disregard FTC Act precedent. For example, in *Island Tobacco Co., Ltd.* v. *R. J. Reynolds Co.,* 627 P. 2d 260 (Hawaii 1981), the Supreme Court of Hawaii ruled that the plaintiff need not show that its private action under the state statute was in the "public interest," as proceedings by the Commission under the FTC Act must be (15 U.S.C. §45(b)). The court stated that while federal law may be used to guide state courts, it must be interpreted in each case in light of and in accordance with conditions in the state. See also *Singleton* v. *Pennington,* 568 S.W.2d 367 (tex. Civ. App. 1978). But see *Lightfoot* v. *McDonald,* 86 Wash. 2d 33, 544 P.2d 88 (1976), holding that private plaintiffs must allege injury to the public to maintain an action under the state act.

In *Bartner* v. *Carter,* 405 A.2d 194 (Me. 1979), the Supreme Court of Maine recognized that the state had intended to bring federal interpretations of unfair and deceptive acts and practices into the state act, to give clear guidance to Maine courts in the construction of those terms. Nonetheless, the court found that differences between the federal and state acts make it impossible to apply federal FTC Act principles to private actions under the state act. The court declined to define deception in terms of "capacity to deceive" because under the state statute, the plaintiff in a private action was required to show actual loss. The court noted that the primary purpose of the FTC Act is preventive, while providing compensation to injured parties is a primary purpose of the state act. For this reason, said the court, federal decisions offer uncertain guidance in the interpretation of the Maine statute's private remedial provisions. See also *State ex rel. Edmisten* v. *J. C. Penny Co., Inc.,* 292 N.C. 311, 233 S.E.2d 895 (1977). Cf. *Moore* v. *Goodyear,* 364 So. 2d 630 (la. App 1978); Comment, Maryland's Consumer Protection Act: A Private Cause of Action for Unfair or Deceptive Trade Practices, 38 Md. L. Rev. 733, 757 (1981).

Courts have felt it necessary to disregard FTC Act precedent to a greater or lesser extent in a variety of other situations. In *Perlman* v. *Time Inc.,* 64 Ill. App. 3d 190, 380 N.E.2d 1040 (App. Ct. 1978), for example, the court held that the Illinois Consumer Fraud Act could prohibit representations made in an advertising plan which had been approved by the FTC. The case involved the defendant's plan to offer Life magazine subscription holders subscriptions to its other publications on a pro rata basis when Life stopped circulation. The use of the conversion formula that Time, Inc. planned to use had been approved by the FTC, and a section of the state statute provided that the act did not apply to advertisements which complied with rules and regulations of the Commission. The court, in overturning a summary judgment for the defendant, ruled that even though the FTC may have approved the use of a certain practice, the state could investigate the representations made in connection with the practice. 380 N.E.2d at 1046.

In *Purity Supreme, Inc.* v. *Attorney General*, 407 N.E.2d 297 (Mass. 1980), the validity of regulations issued by the attorney general under the state consumer-protection statute was at issue. The act required the attorney general's regulations to be "not inconsistent" with rules of the Federal Trade Commission, and the court held that the attorney general was free to adopt rules which were more restrictive than FTC practice. This case involved the use of the Universal Pricing Code, under which prices of grocery items are printed in computerized code on product packages, eliminating the need for marking prices on each item by hand. Although the FTC had approved the use of this practice, the court ruled that the Massachusetts Attorney General could require human-readable prices to be marked on each product. State rules are not inconsistent with FTC rules, stated the court, so long as the FTC has merely permitted, and not required, a practice which is inconsistent with the state rule. 407 N.E.2d at 301.

A number of courts have held state consumer protection statutes to apply to practices which the FTC has chosen not to regulate, or which fall outside the Commission's jurisdiction. In *Murphy* v. *McNamara*, 36 Conn. Supp. 183, 416 A.2d 170 (Super. Ct. 1979), the court held that state courts have the power to declare practices to be deceptive or unfair in violation of the state statute even though the FTC had never ruled on such practices. The statute in that case had recently been amended to provide that "due consideration and great weight" should be afforded to federal interpretations of the FTC Act, but this was held to be no impediment to state courts in construing the state act.

Courts have held state consumer-protection statutes to apply to a variety of businesses which fall outside the jurisdiction of the FTC. These statutes have been held to apply to medical malpractice, *Jones* v. *Sportelli*, 166 N.J. Super. 383, 399 A.2d 1047 (1979); utility rate charges, *Lowell Gas Co.* v. *Attorney General*, 79 Mass. Adv. sh. 49, 385 N.E.2d 240 (1979); household goods movers practices, *American Transfer & Storage Co.* v. *Brown*, 584 S.W.2d 284 (Tex, Civ. App. 1979); insurance claims processing, *Salois* v. *Mutual of Omaha Ins. Co.*, 90 Wash. 2d 355, 581 P.2d 1349 (1978), *Dodd* v. *Commercial Union Ins. Co.*, 365 N.E.2d 802 (Mass. 1977); and landlord-tenant relationships, *Love* v. *Pressley*, 34 N.C. App. 503, 239 S.E.2d 572 (1977), *York* v. *Sullivan*, 369 Mass. 157, 383 N.E.2d 341 (1975).

(2) Congressional amendment of the FTC Act would have no more effect on state enforcement than does federal administrative or judicial interpretation of the Act.

Standing by itself, the vague prohibition against "unfair methods of competition and unfair or deceptive acts or practices" of Section 5(a)(1) of the FTC Act does not provide an adequate standard of enforcement. The generality of this language has been compared to Section 1 of the Sherman Act. Mass. Gen. Laws Ann. ch. 93A comment at 61 (West Supp. 1981). As in the case of Section 1, reliance has been placed on administrative and judicial interpretation to give meaning to the statutory terms and a substantial body of case law now defines them, sometimes in ways the statutory language might not have led one to expect. See, e.g. *Montgomery Ward & Co.*, v. *FTC*, 379 F.2d 666, 670 (7th Cir. 1967) (advertisements considered deceptive if they have the "tendency or capacity" to deceive); *Charles of the Ritz Distrib. Corp.* v. *FTC*, 143 F.2d 676, 680 (2d Cir. 1944) (ads which mislead the "most susceptible" person may be considered deceptive).

This process of interpretation has at times caused very abrupt changes in our understanding of the statute. A case in point would be the Supreme Court's decision in *FTC* v. *Sperry & Hutchinson Co.*, 405 U.S. 233 (1972), in which the Court held that practices may be "unfair" without being either deceptive or anticompetitive. Until that decision, there had been a general belief that the addition of the term "unfair" in the Wheeler-Lea Amendment in 1938 had been mere redundancy. See Little FTC Act: The Neglected Alternative, 9 John Marshall J. 351, 355 (1976). For a full discussion of the process by which the FTC moved, step by step, to the "*S & H* criteria," see Averitt, The Meaning of "Unfair Acts or Practices" in Section 5 of the Federal Trade Commission Act, 70 Geo. L.J. 225, 239-245 (1981).

The necessity of deciding whether or not to adopt new federal precedent arises in the states whenever the Commission or a federal court places a new interpretation on the federal act. States will face no more difficult decision should Congress amend the Act itself. State legislatures, enforcement authorities and courts will be required to determine the extent to which they choose to be bound by Congressional clarification of the FTC Act just as they have been in the past in the face of administrative or judicial interpretation of the Act. The need for policy decisions of this nature, anticipated and accepted by the states in loosely modeling their consumer-protection statutes upon FTC Act, has not constrained the FTC or the courts as they have construed the Act and should not inhibit Congress from amending the federal statute.

Congressional amendment would not, as has been claimed, increase state litigation costs. Any additional litigation expense which results from the relation between state and federal consumer-protection law is due to the fact that states have chosen to model their statutes on the FTC Act but have not, on policy grounds, made them co-extensive with the FTC Act. This circumstance creates uncertainty as to what aspects of federal law will or will not apply in the state. State prosecutors or injured consumers argue for or against the relevance of federal law depending on its effect on their case, and persons charged with violations of state consumer-protection statutes do likewise. This expensive process of testing federal principles in state courts, acquiesced in by the states today for what are deemed to be good and sufficient reasons, would not be greatly exaggerated by Congressional amendment of the FTC Act.

Arguments that Congressional amendment of the Act would reduce the ability of those subject to state statutes to know what conduct is prohibited are similarly without merit. Such uncertainty as exists is not and will not be due to changes in the federal Act, whether those changes result from administrative, judicial or legislative action, but to the ambigious relationship between federal and state law. As has been shown, those subject to state consumer-protection statutes cannot reasonably look to interpretation of the federal act to determine what conduct is or is not permitted by a state act. it is rhetorical nonsense to say that amendment of the federal Act would impair an ability they do not have.

(3) Decisions by state legislatures to relate state law to federal law should not inhibit Congress from amending a federal statute.

There can be no serious argument in principle that state legislative acts may constrain, even morally, the Congress of the United States. When acting within its enumerated powers, the federal government is supreme. *McCulloch* v. *Maryland,* 17 U.S. 406 (1819). States do not freeze a federal statutory scheme in its statuts quo by electing to model state acts upon it. Nor can there be any serious argument that the Federal Trade Commission may constrain Congress by encouraging states to relate their consumer-protection statutes to federal law. Amendment of the FTC Act is appropriate whenever Congress determines that amendment is in the public interest. While Congress may attempt to balance state and federal interests, it must recognize that those interests diverge. The FTC Act serves federal purposes, and those purposes must control when state and federal interests cannot be reconciled.

APPENDIX

STATE CONSUMER PROTECTION LAWS

Statutory citation (et seq.)	All section 5 prohibitions	Unfair and deceptive practices	False, misleading, deceptive, fraudulent	Itemized practices	Unconscionability	Private actions	Regulations	Reference to FTC or Fed. law
Ala. Code tit. 8 § 19-1				X	X	X		X
Alaska Stat. § 45.50.471	X			X		X	X	X
Ariz. Rev. Stat. Ann. § 44-152			X				X	X
Ark. Stat. Ann. § 70-901			X	X			X	
Cal. Civ. Code § 1750 Cal. Bus. & Prof. Code § 17200	X		X		X	X		
Colo. Rev. Stat. § 6-1-101				X		X	X	
Conn. Gen. Stat. § 42-110	X					X	[1]X	X
Del. Code Ann. tit. 6 §§ 2511, 2531			X	X				
D.C. Code tit. 28 App. § 1				X	X	X	X	
Fla. Stat. Ann. § 501.201	X					X	[1]X	X
Ga. Code § 106-201		X		X		X	[1]X	X
Haw. Rev. Stat. § 481A				X		X	X	
Idaho Code § 48-601	X			X		X	[1]X	X
Ill. Rev. Stat. ch. 121 1/2 §§ 261, 311	X			X		X	X	X

STATE CONSUMER PROTECTION LAWS—Continued

Statutory citation (et seq.)	All section 5 prohibitions	Unfair and deceptive practices	False, misleading, deceptive, fraudulent	Itemized practices	Uncon-scionability	Private actions	Regulations	Reference to FTC or Fed. law
Ind. Code Ann. § 24-5-0-.5-1				X		X		
Iowa Code Ann. § 713.24			X				X	
Kan. Stat. § 50-623			X	X	X	X	X	
Ky. Rev. Stat. § 367.110			X		X	X	X	
La. Rev. Stat. Ann. § 51:1401	X					X	X	
Me. Rev. Stat. tit. 5 § 206	X					X	X	X
Md. Com. Law Code Ann. § 13-101		X		X		X	X	X
Mass. Gen. Laws Ann. ch. 93A	X					X	[1] X	X
Mich. Comp. Laws § 445.901		X		X	X	X	X	
Minn. Stat. Ann. § 325				X		X	X	
Miss. Code Ann. § 75-24-1	X			X		X		
Mo. Ann. Stat. § 407.010			X			X		
Mont. Rev. Codes Ann. § 85-401	X					X	[1] X	X
Neb. Rev. Stat. § 59-1601	X			X	X	X		
Nev. Rev. Stat. § 598.360				X				
N.H. Rev. Stat. Ann. § 358-A:1	X			X		X	X	X
N.J. Stat. Ann. § 56:8-1			X		X	X	X	
N.M. Stat. Ann. § 49-15-1		X		X	X	X	X	X
N.Y. Gen. Bus. Law § 349			X		X	X		X
N.C. Gen. Stat. § 75-1	X					X		
N.D. Cent. Code § 51-15-01			X				X	
Ohio Rev. Code Ann. § 1345.01		X		X	X	X	X	X
Okla. Stat. Ann. tit. 15 § 751				X				
Or. Rev. Stat. § 646.605		X		X		X	X	
Pa. Stat. Ann. tit. 73 § 201-1	X			X		X	X	
R.I. Gen. Laws § 6-13.1-1	X			X		X	X	X
S.C. Code § 39-5-10	X					X	X	X
S.D. Comp. Laws Ann. § 37-24-1			X	X		X	X	
Tenn. Code Ann. § 47-18-101	X			X		X		X
Tex. Bus. & Com. Code Ann. tit. 2 § 17.41			X	X	X			X
Utah Code Ann. § 13-11-1			X	X	X	X	X	X
Vt. Stat. Ann. tit. 9 § 2451(a)	X					X	[1] X	X
Va. Code § 59.1-196			X	X		X		
Wash. Rev. Code § 19.86.010	X					X		X
W.Va. Code § 46A-6-101	X			X	X	X	X	X
Wisc. Stat. Ann. §§ 100.18, 100.20	X		X		X	X	X	
Wyo. Stat. § 40-102				X		X		

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[1] Statute requires that rules be consistent with FTC rules.

OFFICE OF THE ATTORNEY GENERAL,
Tallahassee, Fla., September 29, 1982.

Hon. ROBERT KASTEN, Jr.,
Chairman of the Senate Consumer Subcommittee,
Washington, D.C.

DEAR SENATOR KASTEN: I have recently learned of the above proposals now before Congress seeking to change the definition of "unfair and deceptive trade acts and practices" under Section 5 of the Federal Trade Commission Act. After much consideration, I am convinced that a preferable and better course of action would be for Congress to place any necessary limitations of the F.T.C.'s activities or jurisdiction by appropriate legislation directed to such jurisdiction or activities, rather than changing the definition of an established consumer concept. I am confident this alternative will result in less confusion among Federal and state consumer enforcement agencies and will best serve the interests of the consumer and businessmen.

It should be kept in mind that abundant case law arising out of the F.T.C. Act has established a clear definition of "unfair and deceptive acts and practices," based on the premise that any practice that has a tendency or capacity to deceive is subject to proscription. In particular, I would draw your attention to the leading U.S. Supreme Court case of *F.T.C.* v. *Sperry & Hutchinson,* 405 U.S. 2331 (1972). Also, like similar legislation in many other states, Florida's "Little FTC" Act (Chapter 501, Florida Statutes) depends heavily on its parent Federal act, with Federal standards and case law carrying the highest degree of persuasiveness in Florida courts.

Furthermore, the adoption of the proposals now before Congress would certainly signal a return to the "caveat emptor"—buyer beware—principles of the last century. This would mean a re-establishing of the common law tort standard of proving actual damages. Although it was found to be acceptable in earlier times, the common law standard could not effectively accomplish the overriding need to protect consumers from injury. Therefore, it became necessary to establish a remedy that would vest prior to the occurrence of any actual injury and that would make the misrepresentation or fraud itself, and not the resulting injury, the triggering mechanism. Recognizing the inadequacies of the common law standard, Federal and state governments (over the past sixty-eight years) have enacted legislation adopting the new standard as the fair and equitable solution to a growing problem.

If, however, the former standard is now revived, little if anything will be able to curb the activities of unscrupulous advertisers until some unwary consumer suffers actual provable damages. Moreover, with the revival of the common law standard, most violations will be exceedingly difficult to prove because, unlike criminal wrongs, consumer wrongs often do not lend themselves to sensory detection. Indeed, with the ever-growing number of "fly-by-night" operations, the burden of proving actual damages would foreclose any hope of successfully prosecuting the wrongdoers. Therefore, without the power to restrain these activities prior to the infliction of damages, consumer enforcement agencies will be emasculated.

Another proposal now before Congress contained in the above referenced legislation would make the "reasonable" consumer, rather than the "unwary" consumer, the standard for determining whether a given act or practice is unfair and deceptive. As with the proposed definition change, this proposal would surely signal a return to the common law tort standard. Because a major consideration in consumer matters has been the protection of the unwary, a change to the "reasonable" consumer standard would unquestionably work a hardship on the uneducated, the underprivileged, the elderly, the very young and the less sophisticated segments of the population. The overall effect could be disastrous.

A return, therefore, to the world of "caveat emptor" and the adoption of the "reasonable" consumer standard would effect a disservice to all consumers, particularly the naive and unwary. Central to consumer law is the proposition that an advertiser must be responsible for the truth of his representations; to deviate from that standard would, I believe, be extremely unwise. If adopted, the above proposals now before Congress could easily set back by half a century the progress that has been made in this field.

Thank you for your consideration of these views.

Sincerely,

JIM SMITH,
Attorney General.

STATEMENT OF THE NATIONAL ASSOCIATION OF MANUFACTURERS

Mr. Chairman, members of the Subcommittee, the National Association of Manufacturers appreciates this opportunity to submit its views on prospective amendments to that portion of the jurisdiction of the Federal Trade Commission relating to "unfair or deceptive acts or practices." As your will recall, the NAM addressed the issue of consumer unfairness in testimony before your subcommittee on March 18, 1982. Although we do not believe that bifurcated legislative action on unfairness and deception is appropriate due to their inextricable statutory linkage, today we submit our views for the record on the subject of the need to clarify the Commission's deception jurisdiction.

The NAM is a voluntary business organization of approximately 12,000 members and has affiliations through its Associations Department and the National Industrial Council with an additional 158,000 businesses. In total, NAM members account for nearly 80 percent of the nation's industrial output and 85 percent of the nation's industrial workforce. As the nation's major manufacturing business trade association, many of our members produce products for consumer use. Advertising is, therefore, used as an integral tool of communication. Similarly, constraints on advertising as applied through the deception jurisdiction of the FTC are of direct consequence to our members.

SUMMARY OF NAM POSITION

The National Association of Manufacturers believes that greater legislative clarification can be achieved with respect to the consumer deception jurisdiction of the Federal Trade Commission. The definition of deception envisioned by the NAM would consolidate existing common law interpretations of deception, inject evolving federal enforcement policies which call for a rational balancing between interests of the marketplace and the consumer, and, ultimately, result in a statute capable of providing constituents with clearer compliance requirements while achieving its legislative purpose. Moreover, the NAM believes that, consistent with the legislative amendments presently acknowledged as appropriate under the FTC's consumer unfairness authority, corresponding amendments to the Commission's deception jurisdiction are imperative. Absent such action, the NAM believes, clarification achieved by amendments to the unfairness section will be sacrificed through renewed emphasis on deception in those cases presently being brought under the unfairness provision.

A consensus is evolving in Congress which supports codification of the consumer unfairness authority of the Federal Trade Commission. Such consensus, as reflected in Section 2 of S. 2499, evidences the growing dislike of statutory ambiguity. The term unfairness, with little additional qualification, has endless jurisdictional application. In the case of the Federal Trade Commission, the term unfairness is a critical part of the agency's mandate. Empowered to prevent acts or practices which are "unfair or deceptive," the FTC has historically construed this to mean that its consumer jurisdiction is composed of two equal parts, and that the words can be used interchangeably. As a result, Commission actions during the past decade illustrate a use of "boilerplate" charges alleging conduct that constitutes neither deception nor unfairness, but both. This blurring of the distinction between these words has resulted in needless confusion. Sudden changes in Commission usage of one term or another, as distinguished from the traditional interchange of words, will likely create further confusion and subtle yet significant enforcement distinctions. Similarly, compliance requirements are likely to be difficult, is not impossible, to predict.

The NAM is concerned that, bearing in mind the years of past Commission allegations and practices, an unfairness amendment will create new meaning and vitality for deception. Commission Chariman Miller, in our view, properly characterized this fear when he stated before this committee that the Commission could well apply a concept "called in physics the LeChateleir principle . . . if you have a balloon and you push on one side of it, things change on the other side of the balloon."

We believe this section of Commission jurisdiction is just such a creature and that legislative division, at this late date, between unfairness and deception will likely prove this principle correct.

As Chairman Miller underscores: "If we admit there is a problem for commercial advertising with respect to unfairness, we also have to think about the possibility that the Commission might go after the same kinds of things under its deception authority. Just because everybody feels they now know what deception is does not mean that the Commission will stay within that definition in the future. That is the reason I think it is good for Congress to make explicit the kinds of standards the Commission should have in that area."

NAM fully shares Chairman Miller's assessment and concerns about the potential application of the "unfair or deception" jurisdiction of the FTC, barring corresponding legislative action on deception. Any review of past Commission actions premised on this consumer authority underscores the potential for abuse. Congress has recognized the legitimate concerns of the business community regarding ambiguity and administrative excess. The business community, members of Congress and the Commission itself (bar one member) all welcome codification of a limitation on unfairness. NAM members strongly support this congressional action. However, when viewing ths section of the FTC's statute in its entirety, congressional action on unfairness is incomplete; and thus an equal number of problems resolved under unfairness may haunt the business community by problems created with the renewed emphasis on deception.

The NAM maintains that the term deception does not defy definition. The common law is saturated with court decisions construing the boundaries of deception. However, these decisions lead yet to another ambiguity—that deception is advertising or other representations "which have the capacity or tendency to mislead." While boundaries are admittedly established, the NAM believes these boundaries defy definition. Chairman Miller pointedly articulated this problem when he stated:

"Under this definition, virtually any ad can be found to be deceptive. This possibility arises because there are virtually no limits on the kinds of claims that are actionable. There are no checks on the reasonableness of the agency's construction of the meaning of the avertising or the injury that the claim might leade to."

These words of Chairman Miller underscore the difficulty of the Commission in drawing parameters of appropriate federal action. Inasmuch as Congress is attempting to define the meaning of consumer unfairness, similar action with respect to deception is clearly in order.

The NAM recommends that language which would directly define the limits of FTC deception actions be immediately put into place. Specifically, the NAM urges Congress to amend the FTC Act to define deception as meaning: "unlawful acts in or affecting commerce which consist of material representation which are: (a) known to be false or made in reckless disregard of their truth or falsity; or, (b) likely to mislead consumers, acting reasonably in the circumstances, to their detriment.

This proposed definition incorporates the accepted common law principles of deception which brings to bear the full powers of the Commission to act against any instances of actual falsehood or intentionally misleading representations. By so providing, the power of the Commission to prevent and punish such deceitful conduct is reinforced and made subject to the full remedial authority of the FTC. The proposed language further provides the foundation upon which future substantiation cases may rest, in that failure to have a reasonable basis in fact, upon which a claim is made, may be actionable as a statement "made in reckless disregard of its truth or falsity."

Part (b) of the proposed language would define the basic standards by which a practice is to be adjudged in violation of the Commission's deception jurisdiction. By using the language "likely to mislead," part (b) moves the Commission more appropriately towards being required to find that consumers are "likely" to be misled. The current standard, "capacity or tendency," plainly lacks this concrete guidance and is one of subjective meaning. This proposed standard, we believe, will perform two positive features in that it will lend itself more to objective application by the Commission and set a basis for the Commission to develop independent evidence that consumers in fact are likely to be mislead by double meaning in an advertisement.

The proposed definition also provides for the standard that consumers must be "acting reasonably in the circumstances," as a precondition to both injury and liability. Therefore, where sellers have acted in good faith, and the consumer comes to grief through misinterpretation, or carelessness, the FTC should be prevented from intervening. This standard does not, in any manner, compromise the protections necessary for so-called "vulnerable" groups. In fact, we believe that this standard would properly permit the FTC to evaluate an advertisement in light of the special circumstances that pertain to such groups. Advertisings intended to deceive persons of unique sophistications would clearly be barred under part (a) of the proposed definition.

The Commission, prior to bringing actions based upon deception, would be required under part (b) to find that a genuine "detriment" to consumers did in fact occur. By this, the proposed language would encourage the Commission to find a threshold wherein injury can be considered so minimal as to discourage the initiation of the enforcement authority of the FTC. While no specific cost/benefit analysis requirement is proposed, the NAM does believe that the requirement to determine "detriments" should be construed as requiring a balancing of interests between the general value of information supplied to the total marketplace and the impact of the deceptive practice on some consumers. Where it is suggested that injury may have occurred or may likely result, we believe that the resources of the federal government should be evaluated against the degree of potential harm, the remedial measures available to consumers themselves, the potential for overriding or offsetting benefits to the general marketplace and the general enforcement priorities of the agency. Absent such a preliminary analysis, we believe, federal action would be premature and the proposed language would discourage such adventures.

Lastly, and perhaps of greatest general significance, the proposed definition in both parts (a) and (b) incorporates a "materiality" requirement. The NAM believes that only representations that relate to the qualities of a product or service that the seller is seeking to market and that actually influence consumer behavior relating to the purchase of the advertised product should reasonably fall within the realm of legitimate federal intervention. This is not to suggest that false advertising which fails to influence consumers is exempt, but is to say that the justification for federal intervention—the power, resources and tools of the FTC—should only be brought to bear where there can be a reasonable basis to believe that consumer behavior will likely be altered due to misinterpretation.

The NAM appreciates this opportunity to comment on the deception jurisdiction of the Federal Trade Commission and would be pleased to supplement this statement with additional materials if so requested.

STATEMENT OF THE AMERICAN ASSOCIATION OF RETIRED PERSONS

A. IN GENERAL

Under current law, any advertisement can be found deceptive "if it has a tendency or capacity to deceive." It is our position that the current definition of deception should remain intact.

Chairman Miller proposes to change this definition by requiring the FTC to establish certain items before a case based on deception could be brought. His requirements are as follows: (1) significant measurable injury to consumers not outweighed by any consumer benefit; (2) a determination that the misleading statements or representations were factual claims and not opinion; (3) a finding that the advertising had a propensity or the capacity to deceive consumers generally, proving that a "reasonable consumer" would have been misled by the advertising. With regard to vulnerable groups, such as the aged, Chairman Miller proposes that (4) FTC protection could only be accomplished by focusing on whether the perpetrator knew, or should have known, that the act or practice was deceptive, regardless or whether or not reasonable consumers were deceived.

Chairman Miller's attempt to alter the meaning of deception has drawn considerable criticism, especially from other members of the FTC. Commissioner Michael Pertschuk states that "it is not surprising that the law of deceptive advertising has evolved slowly and painstakingly through generations of Commission decisions, subject to the intense and careful scrutiny by the Appellate Courts including the Supreme Court. I believe that most legal scholars would affirm that today the law of deception is relatively well settled and provides solid guideposts for those practitioners who wish to remain in compliance with legal and ethical standards."

Commissioner Patricia Bailey states: "It is no trivial matter to alter 44 years of jurisprudence. If the prohibition on deceptive practices is altered, no matter how benign the intentions of those making the change, the natural assumption of the legal community, including state and Federal judges, will be that Congress must have intended somehow to change the actual effect of the law. The inevitable result will be that at least some deceptive practices which are not illegal under current law will become legal, as judges and lawyers are cast adrift from precedent to search for the new law's meaning."

Pertschuk goes on to state that "although it may theoretically be possible to develop a case under Miller's guidelines, it may be as a practical matter impossible to bring. For the expense of developing the evidence Miller wants—especially at the time when we have limited resources—will be prohibitive."

Under Chairman Miller's proposal, it is uncertain whether several FTC cases could have been brought. One is a case involving Anacin's claim that promoted their product as the best pain reliever on the market because it contained an ingredient "most recommended by doctors" for curing minor aches and ailments. The FTC investigated and found the ingredient to be plain aspirin. As a result, it found the ads misleading and deceptive and ordered the campaign halted.

Applying the new Miller criteria to the Anacin case, before the FTC could file suit, it would have to determine that consumers bought the product only because of the ad and that they were adversely affected by their decision—paying substantially more than they would have if they had bought regular aspirin.

Another case which possibly could not be brought under Chairman Miller's proposal is one where the FTC ordered the makers of Fresh Horizons bread to change its advertisements that promoted the bread for its high fiber content. The FTC discovered that what Fresh Horizons failed to mention was that the fiber was not grain fiber contained in most breads, but wood pulp derived from the pulp of trees. The Commission found this omission was misleading and deceptive.

In the Fresh Horizons case, under the new Miller criteria, it would be nearly impossible for the FTC to prove that consumers were harmed by the omission that the fiber was made of wood pulp, because there is no evidence that wood fiber is worse than grain fiber. But even though there may be no physical harm attached, doesn't the public have a right to know what it is purchasing? Doesn't the fact that a particular bread is made from trees instead of from natural grains play a substantial part in the selection process? Aren't there some things consumers need to know about the products they are buying even though the products may not kill them?

The Associations believe that the well established law of deception should be left as it currently stands and that no additions to or deletions from it should be made.

The following is a discussion of each of the elements of deception as proposed by Chairman Miller.

B. MATERIALITY/COST BENEFIT PROPOSAL

Chairman Miller proposes that before a case could be brought by the FTC, there must be demonstrated significant measurable injury to consumers, not outweighted by any consumer benefit. S. 1984 proposes that "unfair or deceptive" be limited to acts or practices which "cause substantial consumer injury that outweights benefits derived from the act." The primary purpose of such a definition is to overrule the current definition of deception since it alters the burden of proof necessary to establish that an act or practice is deceptive. In addition, it opens new vistas for litigation over the proper definition of "substantial injury" or "benefit," and the quantum of proof and acceptable methodologies for establishing values for these new terms. The proposal similarly obscures the precise calculus for determining whether injury is indeed outweighed by costs.

It is our belief that if the cost benefit proposal were enacted, both government and business will expend much time and effort ascertaining the ratio of costs to benefits of a questioned practice. Whatever the result, it is hard to imagine that the investigation and litigation process will be less burdensome with these added features than under present law.

We are less concerned about the size of the injury, and far more concerned about basic fairness. We think it is ridiculous to stop to total up a balance sheet, weighing consumers' losses against business' gains when citizens are being cheated, misled, manipulated and shortchanged.

Under Chairman Miller's proposal, in addition to requiring the Commission to measure the dollar cost of misleading statements, he would have the Commission look only at economic injury to consumers. His proposal, however, does not take into consideration such things as consumer expectations (to be able to rely upon advertisers' representations) and competitors' losses (an advertiser's competitor may be harmed in the millions of dollars, while the consumer may suffer the loss of a couple of dollars).

Chairman Miller cities as an example of a case that could not be brought using the cost-benefit proposal—the 1977 Poligrip case. There, the makers of Poligrip falsely claimed that the denture adhesive helps denture wearers eat foods such as apples without discomfort or embarrassment. Miller states that "this product is cheap, frequently purchased and easy for consumers to evaluate for themselves." As a result, Miller concludes "the FTC is not needed to police the marketplace" in this type of case because consumers will be able to find the deception easily on their own—and with relatively little effect on their pocketbooks.

We disagree. Even though the economic harm to one individual may be relatively small, think of the embarrassment that may have been cause to a grandfather who, at a Sunday church picnic, bit into an apple only to find his teeth drop to the ground when he removed the apple from his mouth. In addition, what Chairman Miller hopes to measure is singular economic harm. What of collective economic harm as a result of the thousands who may have purchased the item as a result of the advertisement? Would not this have a profound economic impact upon Poligrip's competitors who suffered a loss as a result of the deceptive claim? In addition, should not a 75-year old widow be able to rely upon the representations of an advertiser who is making a sales pitch directed at her?

In *FTC* v. *Colgate-Palmolive Co.* the Supreme Court confirmed that for an advertisement to be deceptive, the Commission must find that it will be a material factor in a consumer's decision to purchase a product. However, the Court noted that the Commission need not survey the public to support such a finding, but may infer materiality from all the evidence. We believe that a requirement of actual proof of injury beyond that already required is burdensome, impactical, and unnecessary.

C. FACT V. OPINION PROPOSAL

Under the Miller proposal, the FTC would have to make a determination that the misleading statements or representations were factual claims and not opinions. We strongly object to this. We firmly believe that the proper approach is to look to the effect that a particular representation has upon consumers rather than trying to delineate between fact and opinion.

Our position is predicated upon the premise that in a great number of consumer transactions, the consumers and sellers do not stand on equal footing as to available informaiton. As a result of this "informational imbalance" between consumers and business, consumers are oftentimes prone to believe the representations of the salesperson.

As an example, consider an opinion as to the performance capabilities of a washing machine made by a salesman of 20 years to a grandmother who does washing for 14 grandchildren and has never before purchased a washing machine. Since the salesman obviously knows what he is talking about, the elderly lady is not dealing at an arm's-length transaction with the salesman but must rely upon his representations and opinions, as a result of his longtme experience in the field, as to the capabilities of the machine.

Commission Pertschuk voices his criticism of the fact-versus-opinion proposal as follows:

"I know of no case that the Commission has brought challenging opinions except for those cases in which the Commission has alleged that opinions such as those of scientific experts were designed to lead consumers to believe that the opinion was backed by expert knowledge and experience. If Dr. Michael DeBakey, the famed heart surgeon, were to appear in a cigarette ad claiming that in his measured opinion as a surgeon it was his judgment a particular cigarette cured cancer, Miller's amendment would appear to place such opinion testimony beyond the reach of the Commission's policing powers. I simply disagree that there is any sound public policy advanced by doing so."

We also anticipate that the enactment of a fact-versus-opinion proposal would result in a great deal of litigation centering around the question of when opinion becomes a representation of fact. We feel the preferred approach is to leave the definition of deception as it currently is.

D. REASONABLENESS PROPOSAL

Chairman Miller's proposal requires a finding that the advertising had a propensity or the capacity to deceive consumers generally, proving that a "reasonable consumer" would have been misled by the advertising. We find this proposal unacceptable for a number of reasons.

In the first place, one knowledgeable observer has commented that Chairman Miller's deception proposal and the reasonableness proposal in particular, should be subtitled "The Lawyers' Relief Act of 1982". The primary problem with the reasonable consumer standard espoused by Chairman Miller is that there is none. Predictably it would require years and countless hours of case by case adjudication to define standards of reasonableness, as well as acceptable methodologies of proof. How do you define "reasonableness." Would what's reasonable to a consumer in New England be reasonable to a consumer in Texas? Would reasonableness of consumer conduct be determined for the class of consumers injured by a practice as a whole, or would the law differentiate in degree among various consumers depending on the complexity or sophistication of the product or marketing scheme in relation to the age, intelligence, and prior purchasing experience of the individual consumers in the class?

Foreseeable are clashes of expert psychologists and other behavorial scientists over the arcane question of whether consumers—who might, in a weak moment, be taken in by the deception—should have known better. Chairman Miller's proposal would also impose a new and difficult element of proof which would often shift the focus of litigation from the deceptive act or practice of the business to the conduct of the consumer.

Under longstanding interpretations, a practice is deceptive if it has the capacity to deceive any substantial or appreciable segment of the public. Thus, the FTC and the courts have created a uniform minimum standard of conduct which properly encompasses all likely targets of a marketing effort by a particular business.

This current approach we feel is more acceptable than creating a reasonableness standard.

E. SPECIAL PROTECTION FOR SPECIAL GROUPS PROPOSAL

With regard to vulnerable groups, such as the aged, the poor, the uneducated, Chairman Miller proposes that FTC protection could only be accomplished by focusing on whether the perpetrator knew the act or practice was deceptive, regardless of whether or not reasonable consumers were deceived. Average consumers who act reasonably are apparently protected regardless of whether the business knew of the likely deceptive effect of its marketing. Vulnerable consumers who act in unreasonable or gullible manner, on the other hand, are protected only if the merchant knew or should have known of the effect of the practice. Therefore, ads aimed at the elderly that promote cures for cancer could be attacked under this proposal. While we appreciate the Chairman Miller's attempt to provide special protection for special groups, we object to his basic premise—his deception criteria—that brought him to the special protection proposal.

In the first place, this proposal is another one which alters the current burden of proof. Using this proposal, it would be far more difficult for the elderly to bring cases since they would have to prove intent.

In addition, a mens rea requirement has never been an element of deception under Section 5, and appropriately not. The FTC Act is not a criminal statute. It does not punish the sinner, it simply seeks to protect the consumer. Intent is irrelevant to whether consumers may be injured and, consequently, to whether a company should be ordered to cease and desist from deceiving the public. Moreover, intent is enormously difficult to prove. Therefore, while Miller's proposal purports to provide special protection for vulnerable groups, the impact of this proposal would leave such groups far more vulnerable to exploitation than under present law.

Again, it would take years of litigation to restore any semblance of stability or predictability to the law, as the FTC and the courts seek coherent definitions of reasonableness, vulnerability, and knowledge. More importantly, these proposals are designed to substantially reduce the standards of acceptable business conduct. If Chairman Miller's proposal is adopted, the elderly, the sick, the handicapped, the uneducated, and other regular targets of deceptive practices will suffer their economic losses in face of defenses of good faith, or lack of intent or knowledge.

STATEMENT OF THE AMERICAN RETAIL FEDERATION

The American Retail Federation appreciates this opportunity to comment on the need for a definition of the term "deceptive" as used in Section 5(a)(1) of the Federal Trade Commission Act.

The Federation speaks for all kinds and sizes of retailers, through its member state retail associations in all 50 states, and the District of Columbia, and 32 national retail associations. Through them, ARF represents over a million retail stores employing 13 million workers and contributing over one quarter of the U.S. gross national product.

The retail industry depends on advertising more than any other segment of the business community. Advertising is essential to retailers because the customer relies on the dissemination of useful information to use in their consideration of the selection of a specific product.

Under Section 5(a)(1) of the FTC Act, the Commission has the authority to prohibit "unfair or deceptive acts or practices." Nowhere in the Act, however, is there a definition of what constitutes an "unfair" or "deceptive" practice. Absent such a definition, this language has permitted the Commission to exercise its broad discretion, on a case by case basis, whether a practice is unfair or deceptive.

In recent years Congress has shown great concern over the way the Federal Trade Commission has exercised its authority with respect to "unfair or deceptive" acts and practices. Although the primary thrust of this concern has focused on the Commission's highly subjective application of its "unfairness" authority, serious questions have also been raised about the Commission's approach to deception". In fact, the recently issued Senate Committee on Commerce, Science and Transportation Report[1] on the pending FTC reauthorization legislation (S. 2499), noted that the Committee found merit in various criticisms that had been raised concerning the FTC's "deception" powers, including criticism with respect to the following points:

First, in interpreting the meaning of a particular ad, the Commission has relied on its own expertise of how consumers would understand the ad. Second, the Commission's interpretation of advertising has not always been based on what consumers acting reasonably under the circumstances would understand the ad to mean. Third, the Commission has sometimes acted without evidence that the challenged ad was likely to injure consumers. Fourth, the Commission's decisions may have sometimes harmed consumers, rather than protected them, because they have suppressed thruthful and useful information.

It has become increasingly clear that the broadness of the Commission's discretion stemming from the language in § 5(a)(1) has, in practice, led to problems. It has permitted the Commission staff, with the endorsement of as few as three Commissioners, to characterize almost any conduct that offends their particular sensibilities as unlawful. The Commission has taken the position that by simply exercising its "expertise," it can define the limits of the law without the application of objective standards. As a result of this, and the tendency of reviewing courts to defer to the Commission's "expertise," the Commission and its staff have repeatedly classified conduct as unlawful on the basis of subjective perceptions and personal beliefs, often in disregard of intent or motive and where no adverse economic impact on consumers exist. This result has been especially apparent in the Commission's actions involving allegedly unfair or deceptive advertising.

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[1] S. Rep. No. 451, 97th Cong., 2d Sess. (1982)

As former Commissioner Pitofsky has stated: Why questions of meaning [of advertising] should be submitted to the virtually unreviewable discretion of five commissioners of the FTC has never been articulated. Unlike other instances of deference to regulators as part of the administrative process, there is no reason to believe that commissioners of the FTC have unusual capacity or experience in coping with questions of meaning, nor any indication that successful regulation of advertising requires a balance of related regulatory considerations that commissioners are in a special position to handle.[2]

As specifically noted below, the Commission's actions in recent years has caused consternation in the retailing community and leads ARF to commend this Committee for undertaking a review of this issue.

The FTC's approach to deception goes far beyond well established common law concepts. Under the Commission's doctrine, for example, neither the meaning the seller intended to convey (or recklessly conveyed), nor the reasonable interpretation of the seller's conduct limits the Commission's ability to find fault. Instead, as numerous cases indicate, the Commission has chosen the approach that a seller may be held responsible for any interpretation which it (the Commission), using its own expertise, makes. As noted above, because Section 5(a)(1) enables the Commission to prohibit "deceptive" practices, without providing any guidelines as to what "deception" actually means, there has been, and continues to be, no meaningful judicial review. Reviewing courts have consistently deferred to the Commission's "expertise" in interpreting advertising; in practical terms, the Commission has no burden of proof to carry as to what the advertising actually meant to consumers—reasonable consumers or otherwise.

In fact, the Commission's staff has often obtained summary judgment as to what an ad meant from the FTC's Administrative Law Judge, and had it affirmed by the Commission. A classic illustration of this was Ford Motor Co., 87 FTC 756 (1976). In this case, the headline of the challenged ad claimed that "All 5 Ford Motor Co. small cars got over 26 MPG." The ad also prominently and expressly stated that mileage veries according to maintenance, equipment, total weight, driving habits and so forth, and added that no two drivers, or even cars, are exactly alike. In the face of these disclaimers, the Commission found an implied claim that the average driver would get the advertised mileage. The Commission determined that this was the claim made solely on the basis of its "expertise" to interpret advertising. In so doing, it refused to consider the results of a consumer survey conducted by Ford which showed that consumers understood what Ford was saying.

Another recent example of Commission philosophy is the Kroger Co. supermarket case, D.9102 (9/15/81). In this case Kroger's advertising described the results of its "Price Patrol" in which homemakers surveyed the prices of 100 to 150 items at local supermarkets. The FTC conceded "that the evidence does not dispute Kroger's basic argument that prices were frequently below or equal to those of its competitors." Nevertheless, based on its own expertise, without any other evidence of the ad's meaning, the Commission held the ads were deceptive because they implicitly represented that the surveys were "methodologically sound" and "statistically projectible."

Commissioner Patricia Bailey dissented on the meaning of the Kroger ads. She noted that Kroger made a point of emphasizing the informality of the surveys. She wrote, "the notion that these surveys were 'methodologically sound' and, therefore, 'prove' an overall 'projection' of lower prices is simply, in my view, an artificial construct imposed by a majority (of the Commissioners) on the ads in question." On the merits of bringing the case, she wrote, "I fear that the majority opinion will chill the development of useful comparative price advertising, especially among retail grocers, which is extermely useful to the public, particularly in times of high inflation."

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[2] Pitofsky, Beyond Nader: Consumer Protection and the Regulation of Advertising, 90 Harvard Law Review 661, 678 (1977).

Even when the Commission considers evidence beyond its subjective interpretations, it sometimes finds corroboration for its conclusions on evidence which would fail to meet the burden of proof required in either a common law or a Lanham Act action.[3] In the *Gelb* case,[4] for example, the Commission interpreted an advertisement for permanent hair coloring to represent that no treatment of after-grown hair would be required, resting on a single consumer who testified—after much prodding—that some other consumers might interpret the claim in that way though she herself knew better. In another instance, the FTC staff charged that the Firestone Tire Company's trade name, "Safety Champion" represented that the tire was safer than any other brand, despite a scientific survey establishing that only 1.4 percent of the surveyed consumers so interpreted the same.[5]

In stark contrast is a recent Lanham Act action in which Coca Cola Company sude Tropicana Products[6] alleging that Tropicana was falsely advertising its pasteurized frozen orange juice as fresh because its commercial visually depected Bruce Jenner squeezing an orange and pouring its juice into an opened container of Tropicana Premium Pack juice despite the fact that Jenner also clearly stated:

"Tropicana Premium Pack. For me it tastes freshest. Its pure pasteurized juice comes from the orange. It's the only leading brand not make with concentrated and water."

After reviewing extensive survey evidence as to what consumers understood the advertising claims to mean, the court characterized the ad's tendency to mislead as "insubstantial" and stated that it was "unwilling to find that Tropicana's commercial probably tends to mislead as high a percentage as 15 percent of its viewers." The sensible approach taken by the courts in Lanham Act actions, such as the *Tropicana* case, in examining survey evidence concerning how reasonable consumers would interpret the ad should also be required in FTC actions.

The Commission's approach to the law of deception has created an atmosphere in which it is virtually impossible for companies subject to the Commission's jurisdiction, for the courts, for the Congress or for the public to predict with any certainty what the law is. The FTC cases cited above illustrate that significant problems exist because of the broad discretion given the Commission under § 5(a)(1) which has led the Commission to believe that it need not prove its case by evidence. If the legal meaning of an advertisement or other representation is simply what three out of five Commissioners say it means, irrespective of the seller's intent or evidence of reasonable consumer reaction, sellers can never be confident that their conduct will survive FTC scrutiny and consumers will in time receive less information about the goods and services they might wish to purchase.

In short, the FTC's approach creates a "chilling" effect on commercial advertising. Both the *Ford* case—involving ads attempting to provide useful mileage information—and the *Kroger* case—involving ads attempting to provide comparative prices—aptly illustrate this. Uncertainty over what interpretation may be placed on statements discourages substantive advertising and ultimately leads to advertising with more "fluff" than substance. When the Commission challenges advertising that has only a mere "tendency" to mislead a small minority of consumers who might read a statement in an unintended way, it discourages the dissemination of useful information to the majority of consumers who interpret the advertisement in its intended sense. As Commissioner Bailey's dissent in the recent *Kroger* case noted, the order at issue there would "chill the development of useful comparative price advertising . . ." In a society such as ours that operates—thrives—on the exchange of information, what result might a "drying up" of such useful information have?

The broadness of the statutory powers given the FTC permits it to pursue enforcement actions based on its own subjective reactions to seller representations rather than actual consumer reactions and creates a substantial risk of enforcement priorities. Foolish cases involving questionable issues, wasting the limited resources of the Commission, are needlessly brought. Not only is meaningful judicial review of commission action of, perhaps, as few as three unelected officials precluded, but accountability to the Congress and the public as well.

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[3] The Lanham Act provides a private right of action to individuals against competitors who falsely describe or misrepresent goods. Though intent to mislead need not be shown to succeed under the Lanham Act, an action brought under it must meet all the other requirements imposed by the common law, including proof that reasonable consumers will be misled by the advertising and proof of injury.

[4] 33 F.T.C. 1450 (1941), aff'd, 144 F.2d 580 (2d Cir. 1944).

[5] Based on these allegations, an FTC Administrative Law Judge issued an order precluding further use of the "Safety Champion" name, although the FTC itself ultimately reversed on this point. Firestone Tire & Robbert Co., 81 F.T.C. 398, aff'd, 482 F.2d 246 (5th Cir. 1973).

[6] *Coca Cola Co.* v. *Tropicana Products, Inc.*, 538 F. Supp. 1091 (1982).

The above discussion aptly illustrates the critical need for explicit legislative guidance. While ARF does not profess to possess any magical definition of the term "deception" but, instead, properly defers to the Committee, we suggest adoption of a statutory amendment which specifically requires the Commission to prove its case through empirical evidence as is already required under common law and the Lanham Act. Subjective interpretation and minimal, if any, "evidence" of consumer confusion should not suffice to find acts or practices unfair or deceptive. This, we believe, would greatly eliminate the uncertainty in the law and provide everyone with a clearer idea of what types of conduct the Commission should properly seek to regulate. The public would receive useful information, the courts could exercise meaningful judicial review and the Congress could hold the Commission accountable for its actions.

In summary, ARF believes that procedural fairness and sound public policy compel more specificity in § 5(a)(1) with respect to the meaning of a "deceptive practice". We commend the Committee for taking time out of its busy schedule to review this issue and thank the Committee for extending the Federation this opportunity to provide its thoughts on this important issue.

We would appreciate having this statement made part of the official record.

POLICING DECEPTIVE ADVERTISING

STEVEN C. SALOP [1]

Federal Trade Commission Chairman James C. Miller, III, is proposing to limit his agency's power to police "deceptive" advertising. He seeks to do so by requiring proof that an offending ad threatens "material" injury to "reasonable" consumers or, alternatively, to a particularly vulnerable target audience.

Consumer activists, including some of Mr. Miller's FTC colleagues, have reacted as if the Chairman were recommending the virtual legalization of deception.

In the precise formulation Mr. Miller has suggested, that may be only a slight exaggeration. The Law being the Law—imprecision aspiring to absolutes—it is entirely possible that "reasonable" would come to be equated with undeceived. And vice versa.

But, in principle, all Chairman Miller is really asking is that Congress introduce economic criteria into territory too long ruled by ambiguity and overreach. In my opinion, the change is sorely needed.

Mr. Miller is certainly correct in his belief that current law on deception permits FTC lawyers to act on the view, which some of them hold, that advertising preys on consumer guilibility, contributing nothing essential to the economic process.

Starting with this assumption, they regard it as their responsibility to ensure that not one viewer is misled by inaccurate or incomplete claims. They simply do not find it necessary to consider whether those claims inform or misinform most consumers.

However, if you begin, as I do, with the opposite assumption—that truthful advertising enables consumers to make better choices and thus performs a valuable economic function—then it becomes less obvious that it is always in the public interest to ban ads which might mislead a few consumers while informing most others. From this vantage point, the appropriate policy question is whether the injury to the few outweighs the benefit to the others.

In the real world, the evidence is overwhelming that advertising which contains truthful information can help consumers choose among the profusion of products available in the marketplace. With information, consumers can better satisfy their needs.

For instance, some consumers may well be confused by the welter of information they have been receiving via advertising from banks, savings and loan associations, money market funds and investment brokers concerning potential earnings on Individual Retirement Accounts. But imagine the difficulty they would face in making good decisions without the information supplied by newspaper and television ads, brochures picked up at bank and S&L counters, even from junk mail and window posters.

Actions by informed consumers, in turn, tend to induce greater competition among sellers, who must offer lower prices or better quality to gain or keep customers. An example of this is the current competition in extended maintenance being offered on many new cars by major U.S. automakers and some imports.

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[1] The author is currently Professor of Economics at the Georgetown University Law Center. Until June 1981, he served as an Associate Director in the Federal Trade Commission's Bureau of Economics.

The benefits from this increased competition are not restricted to those consumers who carefully sift through the information available in advertisements and make better decisions as a result. They also flow to uninformed consumers whose "average marketbasket" purchases will include a portion of the price and quality improvements competitors offer.

As for the contention that products would be cheaper and better if no one advertised, the evidence from the optometry business seems to show conclusively that this is not the case. A 1980 FTC study showed that in states which banned eyeglass advertising, prices were about 15 to 30 percent higher than in states that allowed it.

The theory relates to ideal situations where information is accurate and complete. The practical problem is that information is never complete, never perfect—not even in law or economics, let alone in advertising.

For example, neither the city or highway fuel economy measures used in automobile advertising gives a perfectly satisfactory picture of how the family sedan is likely to perform under actual driving conditions. Better measures can be conceived, of course. But the numbers can help new car buyers to compare different models.

Information useful to some readers or viewers may confuse or mislead others, depending on how much the reader or viewer knows beforehand. How many are informed or deceived may depend on the nature of the claim.

Almost no one is likely to be deceived by Exxon's metaphorical promise to "put a tiger in your tank." On the other hand, if one brand of margarine touts its superiority over butter in lowering cholesterol, consumers who are unaware of the fact that all margarines are lower than butter in cholesterol may make the mistake of switching from another margarine brand in hopes of reducing their cholesterol intake. They may pay a higher price for the advertised margarine or give up a better tasting brand, and not get a cholesterol reduction.

Advertisers, with the FTC looking over their shoulder, frequently meet the incompleteness problem with disclosures, voluntary or involuntary. Fuel economy claims are hedged "for comparison purposes only" and "your mileage may differ." Exxon might elect to explain that its gasoline does not actually contain essence of tiger. "Danish," pastries could carry a tag proclaiming "not baked in Denmark." Haagen-Dazs might tell us that it is made in New Jersey (or is it Brooklyn) and that the name is a pleasant fiction.

But such disclosures are not cost free. They take up space (or time), adding to the advertiser's expenses and getting in the way of his message.

A 30-second ad requiring a 20-second disclosure isn't likely to sell anyone's product. Indeed, some disclosures may already be at or near the point of vanishing returns.

Returns from disclosure vanish, not diminish, when an advertiser stops giving information in an ad because he has to supply too many footnotes, question marks, and extra verbiage. Or because the particular claim isn't worth the doubts raised by the disclaimer.

An automaker may be willing to incur the trouble for a car that can claim 45 MPG, but will he also do it for one that gets 26 MPG? From a public policy standpoint, the issue is whether most consumers are better off receiving more information with fewer footnotes or whether we prefer ads that avoid substance and emphasize brand image, which is the ususal alternative.

In the margarine example, unfootnoted cholesterol claims probably entice some consumers away from butter and cause others to switch margarine brands. The question to consider is whether more people are better off when a margarine advertiser—if obliged to say that "all margarines are lower in cholesterol than butter"—decides not to give its competitors a free ride and, instead, changes its advertising approach to trumpet "Our Margarine is DEElicious."

These are hardly theoretical problems. They arise because the deceptive advertisements banned by the FTC Act have come to be defined by the FTC and by the courts as ads which have "the tendency or the capacity to deceive."

This definition is broad and vague enough to encompass any advertisement which provides less than perfect information. Since the courts generally defer to the FTC's expertise and since no evidence is required to show anyone has actually been deceived or, if deceived, harmed by the deception, about all that is necessary for the courts has been the FTC's opinion that deception has been committed.

At least in the past, some of the FTC's deception hunters have seemed to have perfect information as their objective. Among their targets for complaint actions have been ads featuring unstated but implied claims and even omissions from ads deemed capable of being misinterpreted by the most gullible readers or viewers.

Chairman Miller's proposal is aimed at curbing these excesses. In general, his idea of striking a cost/benefit balance makes excellent economic sense.

I should add that this basic cost/benefit approach can easily accommodate the desire to punish more harshly those few advertisers who make claims they know to be false. For these cases, I would recommend giving the Commission authority to collect civil penalties equal to treble damages. This should supply the appropriate incentive.

Where the Miller proposal goes awry is in focusing almost entirely on "reasonable" consumers. If the FTC in the past has tended to overlook benefits to consumers who are not confused by imperfect information, Mr. Miller errs in the opposite direction. Unless they are targeted as a special audience, his proposal overlooks injuries to "unreasonable" consumers. But these consumers also deserve to be protected. (Indeed, as previously noted, the danger is that a deceived consumer will automatically be classified as unreasonable.)

Consider, for example, a health insurance ad which arrives in the mail and resembles a computerized bill. Suppose market research tests disclose that consumers under the age of 65 recognize the "bill" as an advertisement and consider it "clever," "arresting," "a whale of a good ad." Suppose also that some elderly consumers mistakenly sign up for the insurance, thinking it a bill that needs to be paid.

Mr. Miller's proposal would presumably treat this ad as deceptive if targeted to the elderly but not if it went mainly to a younger audience, even though some elderly might receive it. It is difficult to see, however, why the potential injury to the elderly ought to be ignored because "reasonable" consumers under 65 for whom the ad was intended have no difficulty recognizing it as an advertisement.

My view is that the law should not be geared to the gullible but neither should their susceptibility be altogether ignored.

Fortunately, Chairman Miller's proposal is easily fixed. Protection should be extended to all consumers, and the concept of "net" injury—total costs and injuries exceeding total benefits—should be used to determine whether an offense has been committed.

The distinction between "fact" and "opinion" can also be dropped. Under Mr. Miller's proposal, opinions can never be deceptive by definition. Under this standard, anyone who is deceived by an opinion is treated as unreasonable. Apparently, Chairman Miller believes that no "reasonable" person would ever be taken in by a mere opinion. At the risk of being called unreasonable, I must disagree.

The net injury standard I am recommending would ease the vulnerability of advertisers. But it would still require them to test their advertising copy and their products to substantiate the meanings which a significant number of consumers might derive from a particular ad. "Reasonable" advertisers should be quite willing to live with this requirement.

Although Chairman Miller might disagree, my experience as a former FTC advertising regulator is that ad substantiation programs are a good idea. They are reassuring to advertisers and to publishers of advertising, and they halp consumers know who to trust.

In principle, substantiation might be made voluntary. This would place less of a burden on those advertisers who believe their reputations are substantiation enough. However, advertisers who do substantiate should be allowed to distinguish themselves from those that do not. Even if substantiation were optional, virtually all advertisers might well choose to substantiate their claims. How many advertisers would be willing to disclose that their claims were unsubstantiated?

I believe that Congress needs to draw a line midway between Caveat Vendor and Caveat Emptor. Right now the law is too close to one extreme. Chairman Miller's approval is too close to the other. Mine is aimed at finding a middle ground where advertising isn't judged solely by its effect on the most gullible folks around but where they aren't completely left out of the safety net either.

FEDERAL TRADE COMMISSION REGULATION OF DECEPTIVE ADVERTISING: SHOULD ITS AUTHORITY BE DEFINED BY STATUTE?*

ABSTRACT

In connection with the Federal Trade Commission's 1982 reauthorization, a number of proposals have been advanced, principally, to address the business com-

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*Bruce K. Mulock, Analyst in Business/Government Relations, Economics Division, Congressional Research Service, The Library of Congress, June 15, 1982.

munity's perception that there need to be further checks on the agency's statutory authority to prohibit unfair and deceptive practices in the marketplace. This report examines three proposals to define by statute the FTC's jurisdiction over deceptive trade practices.

SUMMARY

The Federal Trade Commission (FTC) is the principal Federal agency concerned with the regulation of advertising. In recent months, three different proposals have been advanced that would define by statute the FTC's authority to police deceptive acts or practices, including deceptive advertising.**

Proponents of these proposals maintain that it is time for Congress to set limits on what they see as the Commission's present virtually unlimited discretion in deciding what is or is not deceptive. They believe that a narrowing and redefining of the FTC's authority in this area would enable advertisers to know with much greater certainty what is permissible, assist the agency in using its resources more effectively, and prevent any future runaway Commissions from harassing business.

Those who oppose changing the status quo maintain that decades of FTC orders and judicial decisions have established with a substantial degree of certainty the concept of deception. They hold that not only is a redefinition of deception unnecessary, it is highly undesirable. It would result in considerable legal mischief, make the prevention of deceptive practices more difficult, time-consuming and costly, and jeopardize the enforcement of State consumer laws which are modeled on the Federal law.

FEDERAL TRADE COMMISSION REGULATION OF DECEPTIVE ADVERTISING: SHOULD ITS AUTHORITY BE DEFINED BY STATUTE?

THE FTC AND ADVERTISING REGULATION

The Federal Trade Commission was created during the early part of this century (1914) chiefly to address the problems associated with the creation of large and powerful industrial trusts. At its inception and during its early years, consumer protection, including protecting consumers against deceptive advertising, was not initially one of the agency's principal concerns.

Nevertheless, the Federal Trade Commission Act (38 Stat. 717) provided the basic statutory authority upon which the agency through a slow, evolutionary process has assumed its present-day importance in the field of advertising regulation.[1] Specifically, Section 5 of the Act gives the Commission its basic mandate by conferring jurisdiction over "unfair or deceptive acts or practices in commerce." The legislative history of the Act indicates that this was to be an expansive grant of authority:

> The committee gave careful consideration to the question as to whether it would attempt to define the many and variable unfair practices which prevail in commerce and to forbid their continuance or whether it would, by a general declaration condemning unfair practices, leave it to the Commission to determine what practices were unfair. It concluded that the latter course would be better . . .[2]

In point of fact, the first case to reach the courts from the newly created Commission involved the regulation of advertising. The Seventh Circuit upheld the power of the FTC to control deception in advertising, declaring that the Commission had authority to "stop all those trade practices that . . . injure competition directly or through deception of purchasers." [3] Thus, promotional advertising quickly became a target in regulation of business practices.

The FTC's efforts to protect consumers from deceptive advertising, however, eventually ran into legal snares during a period when the Supreme Court refused to stretch the literal meaning of the laws already on the books.[4] In 1931, the Court

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**Note: The answer to the question of whether the proposals would "define" or "redefine" deception is that they would do both. The 97th Congress would be "defining" by statute what the 75th Congress intentionally left undefined. By so doing, this Congress would be "redefining" the meaning of deception as it has evolved through 44 years of administrative and judicial decisions construing that term.

[1] For a more thorough historical perspective, see: U.S. Library of Congress. Congressional Research Service. Advertising Regulation by the Federal Trade Commission. Report No. 79-145 E, by Bruce K. Mulock. Washington, 1979. 39 p.

[2] S. Rep. No. 597, 63d Cong., 2d Sess. 13 (1914).

[3] *Sears, Roebuck & Co.* v. *FTC*, 258 F. 307, 311 (7th Cir. 1919).

[4] *FTC* v. *Raladam Co.* 283 U.S. 643 (1931).

dismissed an FTC complaint against a company on the grounds that no matter how false and deceptive an advertisement was, the Commission had no power to enjoin it in the absence of an allegation and proof that the advertiser's existing or potential competitors were injured.[5]

The FTC thus found itself in an unsatisfactory position. While it would not be particularly difficult to prove the requisite competitive effect in the typical advertising case involving a dishonest advertiser who competed with other advertisers who truthfully represented their competing goods or services, it may have been powerless to deal with instances where the products were unique or where all competitors were making similar false claims. Consequently, the FTC appealed to the Congress for new authority. That authority was conferred as part of the Whealer-Lea Amendment to the Federal Trade Commission Act.[6] The important Section was rewritten to read: "(a)(1) Unfair methods of competition in commerce, and unfair or deceptive acts or practices in commerce are hereby declared unlawful."[7] The addition of the phrase "unfair or deceptive acts or practices" made it no longer necessary for the Commission to show that competition was injured. If there was injury to the public, the FTC was empowered to act.

The legislative history of the amendments affords strong evidence that the Congress believed the new Section 5 prohibition of "unfair or deceptive acts or practices" (as well as special sections covering the advertisement of food, drugs, medical devices, and cosmetics) provided the Commission ample authority to regulate advertising:

> The definition is broad enough to cover every form of advertising deception over which it would be humanly practicable to exercise Government control. It covers every case imposition on a purchaser for which there could be a practical remedy.[8]

The Whealer-Lea Amendment had no discernible effect upon the FTC's approach to advertising regulation nor did it affect in any particular way the standard which the agency employed to judge advertising. The term "unfair or deceptive acts or practices" was not plucked from thin air by the 75th Congress; rather, it sought to codify the standard which the Commission and the courts had developed in prior advertising cases. Those cases had uniformlly held advertising was an "unfair method of competition" not only when it was in fact misleading or deceptive, but also when it had the tendency or capacity to deceive.[9]

PROPOSALS TO DEFINE DECEPTION

For several years, a number of industry trade associations, including advertising associations, have argued that business lives in jeopardy as long as the FTC has the power to use the undefined "fairness" standard to judge advertising and marketing practices. Still angered over the children's TV advertising fight (the so-called "KIVID" controversy), these groups would like to see a continued shrinking of the Commission's powers which began during the last agency reauthorization (1980).[10]

Most observers fully expected that this year's reauthorization process would thoroughly examine and impose restriction on the agency's authority to act on the basis of "unfairness." What was not expected was a major effort to define, and thus narrow, the Commission's power over deceptive advertising.

In late February of this year, Tim Muris, director of the FTC's Bureau of Consumer Protection, told members of the advertising industry that their real problems could not be cured simply by dealing with the unfairness issue.[11] Within three weeks, Mr. Muris' views were being espoused by his boss, FTC Chairman James C. Miller III. Warning that "virtually any ad can be found deceptive" unless Congress intervenes, the Chairman said:

> Should advertisers achieve their goal—the elimination of our unfairness jurisdiction over commercial speech—they would discover they had won a battle but lost the war. Unfairness is only half the critical phrase of our statute. The other half is deception. It, too, needs attention as a legal concept. Indeed, with respect to advertising, almost anything the agency has ever done, or proposed to do under its unfairness jurisdiction, could have been addressed under a deception theory.[12]

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[5] How Government regulates advertising. Advertising Age. November 21, 1973. p. 144.

[6] 15 U.S.C. § 45.

[7] In 1975, "in or affecting commerce" was substituted for "in commerce." Public Law 93-637.

[8] H.R. Rep. No. 1612, 75th Cong., 1st Sess. 5 (1937).

[9] See, for example, *FTC* v. *Hiers Turner Glass Co.*, 81 F. 2d 362, 364 (3d Cir. 1935).

[10] Gordon, Richard. Advertising Age, March 1, 1982. p. 1 and 76.

[11] Ibid., p. 1.

[12] Miller, James C. Why FTC curbs are needed. Advertising Age, March 22, 1982. p. 3.

At about the same time, the National Association of Manufacturers (NAM) and the U.S. Chamber of Commerce put forth their own proposal. This, in turn, was followed by yet another proposal by the three major advertising associations.

Chairman Miller's proposal

Statutory changes are needed to correct three key problems presently existing on just what constitutes deception, according to Chairman Miller. Noting that the Commission has frequently pursued many cases on the grounds of both unfairness and deception, Mr. Miller admonishes that "if we admit there is a problem for commercial advertising with respect to unfairness, we also have to think about the possibility that the Commission might go after the same kinds of things under its deception authority. Just because everybody feels they know what deception is does not mean that the Commission will stay within that definition in the future." [13]

Chairman Miller proposes that the Commission be able to act against deception only when it can show that an ad causes consumer injury, that it is likely to deceive "reasonable" consumers and not just the gullible, and that the deception involves factual claims rather than "opinion." An ad that did not deceive the "reasonable" consumer could still be challenged as deceptive, but only if the advertiser "knew or should have known" that it would deceive "vulnerable" consumers.

NAM and Chamber of Commerce proposal

In December 1980, in response to a request by the Senate Commerce Consumer Subcommittee, the FTC submitted a "Statement of Policy" concerning the scope of its consumer unfairness jurisdiction. The NAM and the Chamber of Commerce have proposed that the principles articulated in the statement be codified so as to define both "unfair" and "deceptive" acts or practices under Section 5 to be those which: directly cause or may forseeably result in substantial economic injury to consumers and such injury is neither reasonably avoidable by consumers themselves nor outweighed by countervailing benefits to consumers or competition * * *.[14]

Advertising industry proposal

Following three weeks of private deliberations among themselves and with key advisors of FTC Chairman Miller,[15] the major advertising associations announced their own proposal to narrow the broad authority Congress gave the Commission in 1938 to regulate deceptive practices. Having stated only a week before Mr. Miller made his proposal that they preferred that Congress "leave the final word on the concept of deception with the courts, where it now lies," [16] the American Advertising Federation, the Association of National Advertisers, and the American Association of Advertising Agencies recommended amending the FTC Act so as to declare that deceptive acts or practices be unlawful if they:

1. Consist of material representations known to be false or made in reckless disregard of their truth or falsity, or
2. Consist of misrepresentations that directly cause or may foreseeably result in substantial economic injury to consumers acting reasonably in the circumstances.[17]

The ad industry's proposal differs from that put forth by Chairman Miller in at least one substantial respect: it would not exempt opinion claims from Commission challenge. Furthermore, the ad industry proposal does not include the cost/benefit language suggested by the NAM and the Chamber of Commerce.

THE PROPOSED CHANGES IN DEFINING DECEPTION: ARGUMENTS FOR AND AGAINST

The proposals put forth to date contain a number of similarities as well as some significant differences. The singular common denominator, however, is that they all proceed from the assumption that language contained in Section 5 of the FTC Act affords the Commission too much discretion in deciding what constitutes "deception." Therefore this Section begins with a look at the general question of whether the Congress should narrow the FTC's authority to police deceptive advertising.

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[13] U.S. Congress. Senate. Committee on Commerce, Science, and Transportation. Reauthorization of the FTC. Hearings, 97th Cong., 2d Sess., March 18-19, 1982. Washington, U.S. Govt. Print. Off., 1982. p. 11. (Hereafter cited as Reauthorization of FTC.)

[14] Note: A bill (S. 1984) introduced by Senators McClure and Melcher would require a similar showing that a deceptive act or practice "causes substantial consumer injury that outweighs the benefits derived from such an act." Arguments for and against employing a cost/benefit requirement are discussed in the following section.

[15] Gordon, Richard L. Ad Industry to back Miller's FTC cutback. Advertising Age, April 19, 1982. p. 1.

[16] Miller's FTC plan draws fire. Advertising Age, March 22, 1982. p. 1.

[17] Gordon. Ad industry to back Miller's FTC cutback. p. 84.

Pro/con arguments concerning specific elements of the major proposals follow, in turn.

GENERAL ARGUMENTS CONCERNING NEED TO DEFINE DECEPTION

Pro

It is time to describe, that is, to specify the FTC's basic mission. It is time Congress set limits on what is now virtually unlimited authority. Broad power in the hands of a few nonelected officials is neither in the public's interest nor, paradoxically, in the agency's interest. Indeed, I believe that one reason the agency has been under so much fire recently is that under Section 5 of the FTC Act three commissioners could just as easily wreak havoc as pursue the interest of the public.[18]

Presently the definition for deception is circular; it says that an ad is legally deceptive if it has a 'tendency or capacity to deceive.' Furthermore, it is overly broad. Under the present definition virtually any ad can be found to be deceptive. This possibility arises because there are virtually no limits on the kinds of claims that are actionable. There are no checks on the reasonableness of the agency's construction of the meaning of the advertising or the injury the claim might lead to.[19]

Because the current Sections legal standard is so broad and ambiguous, case selection has been a time-consuming and recurrent problem.[20]

A body of law should clearly characterize a central core of transactions that will always result in liability. No such understanding exists at the FTC.[21]

Throughout its controversial 68 year history, the FTC has never quite fulfilled its promise of providing consistent and substantial protection to consumers. The fault lies not in the fine people who have served here, but instead in the overly broad standards that Congress has provided us—standards that do not provide guidance on how to proceed. With these broad standards, in one era the Commission did little, focusing largely on trivia. In the next, the Commission took upon itself the mantle of the second most powerful legislature in America, surely a task inappropriate for five unelected officials.[22]

The FTC is an agency of the Congress. The reauthorization process affords Congress, the public, and the Federal agency the opportunity to reconsider the Commission's underlying mandate.[23]

While the Chamber (of Commerce) applauds the emphasis on economic analysis and the respect for market forces brought to the Commission by Chairman Miller and his staff, we cannot ignore the prospect that those contributions may be nullified in the future. We therefore urge the Congress to provide more certain guidance to all future Commissions and to the courts which will review their actions.[24]

As the Commission itself has recently recognized, it is 'entirely proper' for Congress to 'provide as much guidance as feasible to administrative agencies' in the form of more precise statutory standards for the benefit of both the 'regulated' and 'regulator.'[25]

Under current law, the commission can find an ad deceptive not only for what it says but for what it does not say. For example, the commission has required sellers of salt substitutes to state that the products are not appropriate for those on potassium-restricted diets. The commission found the ads to be deceptive and required this disclosure even though the ads made no claims regarding potassium.[26]

Con

To the best of my knowledge, not a single advertiser, advertising agency or advertising medium or any of their trade associations has urged upon the Commission or Congress the statutory redefinition of deception. No previous Chairman or any individual Commissioner suggested it. It is my understanding that no other present member of the Commission supports it. Jeff Joseph, of the U.S. Chamber of Commerce is quoted as saying, "Everyone knows how far you can go with deception.

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[18] Miller. Why the FTC needs curbs. p. 3.

[19] Statement by James C. Miller. Reauthorization of the FTC, p. 11.

[20] Reauthorization of the FTC. p. 81.

[21] Ibid., p. 82.

[22] Statement by Tim Muris, FTC. Reauthorization of the FTC, p. 84.

[23] Reauthorization of the FTC, p. 98.

[24] Statement by Nartub F. Connor on behalf of the Chamber of Commerce of the United States. Reauthorization of the FTC, p. 124.

[25] Ibid., p. 124.

[26] Miller. Why the FTC needs curbs. p. 83.

We've had forty years of it." That the Chairman marches to his own drummer on deception by no means proves that he is wrong, but it is surely grounds for Congressional wariness.[27]

Congress has determined that administrative agencies must possess sufficiently broad legal authority if they are to effectively carry out their responsibilities. This authority has enabled bodies such as the Federal Trade Commission . . . to respond quickly and creatively to the ever changing commercial practices that are characteristic of a dynamic marketplace.[28]

We are told the law needs to be changed so no future runaway FTC will harass honest businessmen. All but unmentioned is the price: The same changes that protect decent businessmen from harassment by Government become the loopholes that expose them to harassment by unscrupulous competitors.[29]

Any catalogue of alleged 'mistakes' the Commission may have made in the last 44 years is really beside the point. No statutory change can ensure that bad cases (assuming we could agree on a universal definition of 'bad') will never be brought; only judicious commissioners, exercising their collective discretion to the best of their ability, guided by Congressional oversight and the Federal courts, can prevent mistakes.[30]

It is no trivial matter to alter 44 years of jurisprudence. If the prohibition on 'deceptive practices' is altered, no matter how benign the intentions of those making the change, the natural assumption of the legal community, including State and Federal judges, will be that Congress intended to change the actual effect of the law. The inevitable result will be that at least some deceptive practices which are now illegal under current law will become legal, as judges and lawyers are cast adrift from precedent to search for the new law's meaning. Only one thing is certain—any change will be a bonanza for lawyers. With 44 years of legal doctrine tossed out the window, every new FTC case will have to be decided without the benefit of established precedent.[31]

The consumer protection statutes of 33 States mirror the FTC's prohibition against 'unfair or deceptive acts or practices' (so called 'little FTC Acts') and 13 others declare deceptive practices to be unlawful. State courts have had little problem applying the concepts of unfairness or deception to the ever changing and seemingly limitless types of fradulent business conduct. A definitive body of case law has developed which clearly outlines the parameters of unacceptable business conduct. By now attempting a precise statutory definition, this case law would become obsolete and a free-fire zone to probe and test the new definitions would be created. Instead of injecting certainty and guidance into this area, just the opposite result would be achieved.[32]

Changes in the law do not make the practices themselves less unfair or deceptive. They simply define for the unscrupulous the areas that are beyond the reach of the marketplace policeman.[33]

All of the various proposals ignore the highly significant point that deceptive trade practices is a far wider category than just advertising. Neither the Chairman nor the ad associations (though they more understandably) have concerned themselves in these proposals with their potential impact on the myriad of deceptive practices challenged by the Commission and the States over the years which have nothing to do with advertising. For that reason alone the Congress should hesitate to alter this statutory standard pending at least a review of the impact of a new statute outside the world of Madison Avenue.[34]

Substantial consumer injury should be demonstrable

The FTC currently has an internal policy stating that it is appropriate to take action only against those advertising practices which result in substantial consumer injury. The proposals of Chairman Miller, the Chamber of Commerce and NAM, and the advertising associations would require the agency, by law, to show that an ad causes consumer injury before it could act on the basis of deception.

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[27] Statement by Michael Pertschuk (prior to deception definition subsequently developed by ad associations). Reauthorization of the FTC, p. 223.

[28] Statement by David I. Greenberg. Consumer Federation of America. Reauthorization of the FTC, p. 185.

[29] Cohen, Stanley E. A new law legalizing some deception? Advertising Age, April 19, 1982. p. 50.

[30] Statement by Particia P. Bailey. Reauthorization of the FTC, p. 344.

[31] Ibid., p. 351.

[32] Statement of Bronson C. LaFollette. Wisconsin Attorney General. Reauthorization of the FTC, p. 328.

[33] Cohen. A new law legalizing some deception? p. 50.

[34] Bailey. Reauthorization of the FTC. p. 346.

Pro

The commission currently is not required to find evidence that the challenged act or practice injures consumers. I see no reason to spend taxpayers' dollars unless consumers will be harmed. To remedy this problem, I would suggest a materiality element, as does the common law.[35]

There is another major problem with the commission's discretion with respect to deception. The commission doesn't have to consider if consumers have actually been harmed. The Poli-Grip denture cream case is illustrative. The ad claimed users could eat 'problem' foods. Although this product was inexpensive, frequently purchased and, by its nature, something each consumer could easily evaluate, the commission took issue with the ads. As then-commissioner Thompson put it in his dissent, "It is inconceivable to me that any denture wearer who applied Poli-Grip or Super Poli-Grip and bit into a red apple and then saw his dentures smiling back at him would ever purchase the gripper again." [36]

The Commission should only address practices that are likely to injure consumers. There is no reason to spend the taxpayer's resources, or those of the companies whose practices we challenge, except to protect consumers. When consumers are not likely to be injured, they do not need protection. The FTC should challenge only those practices likely to cause an injury that consumers themselves would reasonably regard as significant. (At common law, this injury test is expressed in the materiality requirement. Materiality has two elements. The consumers must (a) rely on the claim, (b) to their detriment. The statement in the text is another way to express this common law test.)

The key element of likely injury has been largely eliminated from FTC law. To the extent that the Commission must find that consumers are injured, and few cases require such a finding, the Commission's reliance on its own expertise has emasculated the requirement. A requirement that the Commission in fact prove that this kind of injury is likely before it finds an ad deceptive is not a requirement for quantitative cost-benefit analysis in advertising cases. Nor need injury be measured in monetary terms. Rather, in most instances, a logical inference that injury is likely to exist would suffice, subject, of course, to rebuttal by the respondent's evidence.[37]

Con

Even assuming that the Commission could distinguish between cases where a 'logical inference' of injury would be appropriate and those where it would not and that the courts would accept our distinction without question as within our discretion (which is doubtful), some extensive documentation of injury would almost always be necessary to meet the respondent's inevitable evidence that consumers were not materially harmed by the proven deception. Once again, I reiterate that I agree with Mr. Muris that the Commission should focus its limited resources on cases where deception can cause the greatest injury to consumers. But once we have proven a claim is false, or unsubstantiated, we should not also have to examine what the product was really worth to consumers or what opportunities for benefit they missed by buying it rather than some other product.[38]

It is one thing to establish, as the Commission already has, that, as a matter of policy, it is appropriate to take action only against those advertising practices which result in substantial injury to consumers. It is another thing altogether to statutorily bind the commission to such a policy, for to do so would be to deny the Commission the authority to act in situations where exceptions to the policy would be appropriate.

Timothy Muris of Chairman Miller's staff, characterizes the nature of actionable consumer injury as follows:

To determine if consumer injury is likely, the key question is whether consumers have given up something of value if the claim is false . . . [I]t is unlikely that consumers will give up anything of value unless the product is worth more if the claim is true than it is worth if the claim is false.

How can one assign 'worth' to the psychic injury associated with a false claim that a product is kosher or vegetarian when it is not? Moreover, were the FTC prohibited by law from taking action against advertisers in all cases where the product in question would be worth no more were the false claim true, the integrity of the entire marketing process would be threatened. By permitting as a matter of law, seemingly innocuous false and deceptive claims, public perceptions of accuracy in advertising would be irreparably damaged. It would take no more than a small handful of unscrupulous advertisers, unconcerned about the accuracy of their representations in the absence of any threat of public legal sanctions, to destroy public perceptions of legitimacy in advertising and advertising regulation as a whole. A 'free-fire zone' for deceptive advertising would be the inevitable result of adopting Chairman Miller's proposal.

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[35] FTC: Commissioners divieded on redefining "deception." Bureau of National Affairs, Daily Report for Executives, May 4, 1982. p. C-2.

[36] Miller. Why FTC curbs needed. March 22, 1982. p. 3.

[37] Excerpt of memo from Tim Muris to Chairman Miller. Reauthorization of FTC, p. 77.

[38] Statement by Gerald J. Thain. Reauthorization of FTC, p. 312.

In conclusion, what Chairman Miller's proposal fails to recognize is that the law on paper does not always emerge as the law in practice. The hypothetically reasonable consumer is reduced to a useless fiction in a context in which purchasing decisions are swayed by a multimillion dollar industry expert in sophisticated techniques of consumer seduction. A required showing of measurable consumer injury likewise fails to adequately protect the consumer interest in practice.[39]

Deception should involve facts, not opinions

An unfair or deceptive business practice may also be found in statements of the seller's opinion, which often take the form of an overstatement of the qualities and value of the product. But if every such statement of opinion could serve as the basis of a lawsuit by a dissatisfied customer, competitive advertising would be disrupted, comparative information about competing products would become unavailable, and informed consumer choice would be severely limited. For this reason, and because some exaggeration is to be expected, the sales talk or puffing exception to the unlawfulness of false or misleading statements has become well recognized by courts and the FTC. Mr. Justice Holmes expressed the rationale of the rule as follows: "The rule of law is hardly to be regretted, when it is considered how easily and insensibly words of hope or expectation are converted by an interested memory into statements of quality and value when te expectation has been disappointed." Numerous cases affirm the exemption of mere statements of opinion, sales talk, or puffing from the laws of unfair or deceptive business practices.[40]

Alleging that "the Commission has pursued claims that were clearly statements of opinion and not fact,"[41] Chairman Miller has proposed as one of three criteria that the agency be statutorially limited to attacking deception involving factual claims rather than "opinion." Neither the Chamber of Commerce and NAM nor the ad associations have endorsed this approach.

Pro

The opinion-fact distinction is one grounded in the common law. At common law, statements of opinion generally were not actionable, although misstatements of fact were. Statements that are clearly exaggerated, or puffing in nature, should not be actionable, because reasonable consumers would not in fact rely on them. The common law definition of opinion also exempted clearly subjective claims, such as those regarding taste, appearance, or smell.

The Commission definition of "puffery" is more limited than at common law, because the Commission is not limited to reasonable interpretations of advertising claims. Those problems are exacerbated by the Commission's reliance on its own expertise to determine what an ad means, and whether it is mere puffery.[42]

A distinction between facts and opinions is needed. The Commission should not pursue claims about which reasonable persons would disagree if they possessed all the facts, provided that the claim itself gives a fair indication that it is merely opinion. What constitutes a fair indication depends, of course, on the context of the claim. In general, the Commission should not pursue three classes of claims. It should not pursue subjective claims, such as claims about taste or scent. It should not pursue obviously exaggerated claims, such as "put a tiger in your tank." And, it should not pursue correctly stated descriptions of expert opinions, unless there is no reasonable disagreement among experts about the issue. All of these claims are useful to consumers, and seldom, if ever, lead to injury.[43]

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[39] Statement by Patricia P. Bailey. Reauthorization of FTC, p. 344.

[40] Kintner, Earl W. A Primer on the Law of Deceptive Practices. New York, Macmillan Publishing Co., 1978. p. 97.

[41] Testimony of Chairman Miller. Reauthorization of FTC, p. 12.

[42] Response by Chairman Miller to question of Senator Gorton. Reauthorization of FTC, p. 44.

[43] Excerpt of memo from Tim Muris to Chairman Miller. Reauthorization of FTC, p. 73.

The common law distinction between facts and opinions, although primarily encompassing the problems of subjective and obviously exaggerated claims, also provides a basis for analyzing expert opinion. The utility of correctly stated expert opinion should be obvious. It allows consumers access to the conclusions of those more knowledgeable than themselves at low cost.[44]

A representation of an expert's opinion is a factual claim that the expert holds the advertised opinion. Misrepresentations of expert opinion are clearly subject to challenge even within a distinction between fact and opinion. Similarly, it is quite possible to misrepresent the degree of expertise of the source of an opinion. To advertise the opinion of Nobel Laureate Linus Pauling on the benefits of vitamin C, without disclosing that his prize was for his work in physics, is a factual misrepresentation of the nature of his qualifications. It should be actionable, and is, even if opinion claims are generally excepted from the coverage of the statute.[45]

Further, representation of an expert's opinion implies that the opinion is genuinely held. When the expert's judgment is bought and paid for, this implied representation is false, and actionable. Of course, there is an important, albeit sometimes subtle, difference between paying for an honest opinion and buying the outcome. The latter situation is plainly actionable.[46]

Finally, and perhaps most importantly, there are significant checks among experts themselves. All an expert has to sell is his judgment. The value of that judgment depends on the expert's reputation. Experts are seldom willing to squander that reputation, because once they do, they have nothing left to sell. To use Commissioner Pertschuk's example, it is inconceivable to me, on the present state of evidence, that Dr. DeBakey could be induced to endorse a cigarette as a cure for cancer. Such an endorsement would destroy his credibility, and marketability, forever.[47]

Con

The problem with permitting advertisers to rely on other's opinions about objective performance characteristics is that if the advertiser cannot substantiate the opinion, it can nonetheless shop around for someone who will state and unsubstantiable performance claim in opinion form. Then the door is open to virtually any claim, regardless of the ad substantiation doctrine, which Chairman Miller now states he endorses in principle.[48]

A further reason for rejecting the proposal becomes apparent when one asks the question of why such statements are so widely used in marketing and advertising if, as Mr. Muris suggests, they do not materially influence consumer purchase decisions. If one looks beyond the models and literature of economics to reputable scholarship in the related fields of communication and social psychology, the quite obvious answer is found. Statements or representations of 'mere opinion' in fact influence though and decisionmaking processes through various means, the most simple of which is the implication of underlying facts which support the offering of the opinion.[49]

Finally, with respect to the fact/opinion proposal, it must be taken into account that the functions and goals of the common law and the FTCA are really quite different. The common law is retrospective in its view and seeks to redress actual injury which results from the conduct of one person toward another. It is rigorous and narrow in its focus upon what in fact occurred in a given event. The FTCA, however, is prospective in its orientation and has as its goal the prevention of likely injury before it occurs or is compounded by repetition. These fundamentally different outlooks suggest that incorporation of common law rules pertaining to injury caused by the use of fraud or misrepresentation into the jurisprudence of deception under Section 5 ought to occur only after the most careful consideration of the quite different functions of private and public law and an evaluation of the compatibility of a private law rule with the purposes of the public law. The proposed fact/opinion rule transfer in a form not modifed to reflect the quite different function of public law in the area of deception would be, in my view, an egregious mistake.[50]

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[44] Ibid., p. 74.
[45] Ibid., p. 75.
[46] Ibid., p. 76.
[47] Ibid.
[48] Statement of Mark Silbuergeld. Reauthorization of FTC, p. 158.
[49] Statement of Professor David A. Rice. Reauthorization of FTC, p. 258.
[50] Professor Rice. Reauthorization of FTC, p. 259.

"Reasonable" consumers

Chairman Miller's proposal and that of the advertising associations both employ a reasonableness standard. The FTC Chairman has suggested that the agency be permitted to act only where "reasonable" consumers and deceived unless the agency can show an advertiser "knew or should have known" the act or practice would deceive a vulnerable group.[51] The ad associations speak of "consumers acting reasonable in the circumstances."

Pro

Deception law appropriately does not provide for a defense based upon the literal truthfulness of the challenged statements. Clever lawyers and advertisers could string together literally true statements, yet make a false inference nearly irresistible. FTC law has gone to the opposite extreme—clever lawyers can take a statement apart piece by piece, looking for every conceivable implication, without regard for whether it is reasonable.

The reasonableness standard is intended to preclude some of this clever lawyering under the current standard that an ad is deceptive if it has the tendency or capacity to deceive. Moreover, a reasonableness standard would sometimes require additional evidence, beyond the Commission's own expertise. Such a standard, however, would not impose any significant barrier in those cases that the Commission should prosecute. It would not require surveys or other extrinsic evidence in all cases; indeed, such evidence would be necessary only in that small class of "close" cases.[52]

Reasonableness is an ancient and honorable legal doctrine, used by courts and scholars long before reliable public opinion surveys existed. Many areas of law have evolved over the years based on what reasonable people can, and cannot, do under a wide variety of circumstances. Although a different standard from that currently used, reasonable interpretation is thus not likely to be difficult to apply, or will it be foreign to lawyers.[53]

(T)he reasonableness standard would clarify what is now unclear—the standards by which to judge an act or practice. Both the Commission and businesses would benefit from this increased clarity. The standard would place needed limits on Commission action in those cases when the Commission should not act at all. In cases when the Commission should clearly act, the reasonableness standard would not significantly complicate a trial, it would not require evidence of consumer interpretation, and it would not raise significant problems of application. In cases when it is unclear whether the Commission should act, the standard is likely to require the Commission to develop extrinsic evidence to decide whether to proceed. That is as it should be.[54]

Con

Chairman Miller's proposal requires a finding that the advertising had a propensity or the capacity to deceive consumers generally, proving that a "reasonable consumer" would have been misled by the advertising. We find this proposal unacceptable for a number of reasons.

In the first place, one knowledgeable observer has commented that Chairman Miller's deception proposal and the reasonableness proposal in particular, should be substituted "The Lawyers' Relief Act of 1982." The primary problem with the reasonable consumer standard espoused by Chairman Miller is that there is none. Predictably it would require years and countless hours of case adjudication to define standards of reasonableness, as well as acceptable methodologies of proof. How do you define "reasonableness." Would what's reasonable to a consumer in New England be reasonable to a consumer in Texas? Would reasonableness of consumer conduct be determined for the class of consumers injured by a practice as a whole, or would the law differentiate in degree among various consumers depending on the complexity or sophistication of the product or marketing scheme in relation to the age, intelligence, and prior purchasing experience of the individual consumers in the class?[55]

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[51] Pro/con arguments concerning the "knew or should have known" criteria are examined beginning at p. 186.

[52] Muris Memo. Reauthorization of FTC, p. 66.

[53] Ibid.

[54] Ibid., p. 68–69.

[55] Statement of National Retired Teachers Association and American Association of Retired Persons, Reauthorization of FTC, p. 287.

The Chairman's proposal to incorporate a standard of "reasonable" consumer behavior introduces yet another lever for legal mischief. In allocating the Commission's increasingly scarce law enforcement resources, it ordinarily makes little sense to protect consumers against deceptions which are transparent or unlikely to deceive any but the willfully gullible. But incorporating such standards into the Commission's administrative proceedings and appellate reviews as a matter of substantive law would insure that the hearings would dwell, not only on the normal evidence that an advertisement has the capacity to deceive consumers, but also would include clashes of expert psychologists and other behavioral scientists over the arcane question of whether consumers—who might, in a weak moment, be taken in by the deception—should have known better.[56]

Chairman Miller's third point is not unsound, but it overstates the "problem." There are, of course, laughable precedents—veritable strawmen for those who would criticize the FTC for focusing its resources upon the protection of fools against their own irresponsibility. Any serious observer of the Commission knows, however, that the effect of a practice on incredulous, unthinking fools is not the benchmark that the FTC has employed in practice. And although there are indeed cases in which the Commission earned criticism for issuing orders in the face of evidence that a relatively small percentage of consumers had been or would likely be deceived, an examination of the records and opinions of all decided cases and matters resolved by consent order would demonstrate that such cases become celebrated because they are exception rather than the rule. To "cure" the "problem" by enacting legislation is purely and simply overskill, a variant on the well-worn cliche about using an elephant gun to kill a mosquito.[57]

Cost/benefit provision

One of the major standards contained in Chairman Miller's proposal to define deception is that the injury to consumers "should not be outweighed by consumer or competitive benefits resulting from the challenged practice." The U.S. Chamber's and NAM's legislative proposal that injury not be "outweighed by countervailing benefits to consumers or competition" is similar.

Pro

The NAM considers the likelihood of countervailing benefits of great significance in reaching a final conclusion that an FTC prosecution or rulemaking initiative is warranted. The determination of countervailing benefits will force a matter in question to be fully balanced between the potentially harmful act or practice and the net practical benefit to consumers or competition. This balancing of interests would require the Commission to quantitatively and qualitatively reduce its perception of a potential injury by the factors of economic and social costs and benefits that a practice may entail. In reaching this determination of "net" effects, the Commission should account for the costs of a prospective remedy costs to the parties, increased paperwork and regulatory burdens, reduced incentives for innovation and capital formation and other similar considerations.

The NAM views the Commission letter of March 5, 1982, as constructive in this respect and urges Congress to codify the principles and intent of that letter. The Commission's letter states a position wholly consistent with that of the NAM with regard to countervailing benefits:

"* * * the injury should not be outweighed by consumer or competitive benefits resulting from the challenged practice. Clearly, most business practices involve an economic and social mixture of costs and benefits; hence, unless a particular practice has the net effect of being injurious, the Commission should refrain from finding it unfair. In reaching its decision, the Commission should take into account costs related to a prospective remedy, including but not limited to direct costs to the parties, increased paperwork and regulatory burdens, reduced incentives for innovation and capital formation and like matters." [58]

One standard we have proposed for inclusion in the FTC Act is that the injury to consumers "should not be outweighed by consumer or competitive benefits resulting from the challenged practice." This standard sets out a limited cost/benefit analysis that the Commission must perform. That analysis, like other elements in its decision, should be subject to judicial review. Since the relevant factors in the balance will sometimes be complex, and intangible, however, the court should not insist on a precise quantification of matters that may not lend themselves to that treatment.

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[56] Pertschuk, Reauthorization of FTC, p. 224.

[57] Professor Rice. Reauthorization of FTC, p. 259.

[58] Statement of James P. Cartry on behalf of the National Association of Manufacturers. Reauthorization of FTC, p. 102.

Cost-benefit analysis does not require a formal quantification of every variable. It does require that the agency think systematically about the effects of its proposed actions, and that it consider all such effects. In a definition of unfairness, this requirement would mean that the agency must set forth the beneficial and adverse effects of its proposed actions, and have sufficient evidence to conclude that benefits exceed costs before it acts. In some instances, a qualitative assessment will suffice. In other cases, a more elaborate analysis would be necessary. In close cases, such an analysis will enable the agency to reach better decisions.[59]

If a claim is to be considered a worthy candidate for challenge, the answers should have established that it is received by substantial numbers of consumers, that it leads to significant injury, and that market forces are unlikely to remedy the problem. But even this may not be enough. Although Commission action in such a case may produce consumer benefits by improving the accuracy of one aspect of the advertisement, it may on balance make consumers worse off if it incidentally suppresses other truthful claims contained within the advertisement. It is thus necessary to ask about possible offsetting effects on the flow of truthful and useful information before Commission action would seem warranted. When such effects exist, it is of course necessary to evaluate the significance of the information suppressed, in the same way as one evaluates the benefits of eliminating a false or deceptive claim.[60]

Con

The cost-benefit proposal alters burden of proof necessary to establish that an act or practice is deceptive. In addition, it opens new vistas for litigation over the proper definition of "substantial injury" or "benefits", and the quantum proof and acceptable methodologies for establishing values for these terms. The proposal similarly obscures the precise calculus for determining whether injury is indeed outweighed by costs.[61]

The effort to impose a cost/benefit test on FTC advertising cases distorts FTC's role in the advertising field. Cost/benefit is, or course, a legitimate consideration in selecting advertising cases, and the commission traditionally takes it into account. But cost/benefit is only one consideration, and not necessarily the most important one.

FTC's duty is not to the defrauded consumer alone, but to the marketplace itself. The commission is less concerned about the size of the injury than it is about the morality of practices that prevail. It is worth noting that the safety net woven by Caspar Weinberger and Miles Kirkpatrick is made from cases that might not have been possible if they had to contend with the cost/benefit barrier currently under consideration.

Only nominal consumer injury was caused by advertising for Palmolive shave cream, Pfizer's Unburn and Listerine. Yet the ban on phony TV demonstrations, the ad substantiation doctrine and the concept of corrective advertising established by these cases moved advertising ethics from the flim-flam that prevailed in the 1960s to the laudable standards that exist today.

Before going further down this road, I hope the leaders of the advertising business will soberly consider the consequences. My experience persuades me that advertisers who are scrupulous in respecting the rights of their customers and competitors have little to fear from FTC. Yet they are the ones who have the most to lose if loopholes are inserted in the law that make it more difficult for FTC to deal with less socially responsible advertisers.

With the cost/benefit test in place, there will be no help from FTC when companies marketing small-ticket package goods items face less socially responsible competitors using dubious advertising techniques. With FTC removed from the picture, the less scrupulous small-ticket package goods marketer is also free to thumb his nose at self-regulation.

The cost/benefit concept leads to two-tier morality, with tough FTC justice for the auto industry, the appliances industry and other big-ticket items, and sanctuary for the small-ticket package goods marketers. But in the end, as the cumulative impact of unpunished misdeeds by small-ticket advertisers erodes public confidence in advertising, and public respect for advertising people, the entire advertising business bears the consequences.

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[59] Written response from Chairman Miller to questions of Senator Gorton. Reauthorization of FTC, p. 42.

[60] Remarks of Chairman Miller before the American Advertising Federation. Washington, December 8, 1981.

[61] Montgomery. Reauthorization of FTC, p. 141.

Cost/benefit as a statutory test would be less objectionable if there was reason to believe the full meaning of "cost" and "benefit" were understood. For example, will cost/benefit take into account the social disarray that develops when consumers feel they are systematically abused? We are in an era when advertisers are skilled in using the latest social science knowledge to penetrate consumer defenses, and a new media mix is emerging opening the ways for selling techniques yet to be invented. What will the ultimate cost be if FTC lacks the reach to deal with problems as they develop?

And how do we measure "benefit"? Palmolive Rapid Shave, Unburn and Listerine led to a new ethic which encourages consumers to respect advertising people and trust in advertising. Advertisers get a bigger hang for their advertising buck. Prices are lower because effective advertising holds selling costs down. How do these valuable considerations survive once the law is amended so FTC deals only with advertising cases where the injury to consumers exceeds the countervailing benefits?[62]

Knew or should have known

Part of Chairman Miller's proposal, as already discussed, is that the Commission should measure deception by whether "reasonable" consumers are likely to be deceived, not whether any consumers might be deceived. To this he adds, "This does not mean that the Commission should never protect vulnerable groups. With respect to vulnerable groups, such protection could be accomplished by focusing on whether the perpetrator *knew or should have known* that the act or practice was deceptive, regardless of whether or not reasonable consumers were deceived."[63] A large number of cases have affirmed that under present law, the motive or innocence of a misrepresentation is irrelevant in a suit by the FTC alleging deceptive business practices.[64]

Pro

Under the reasonableness test, the Commission will be able to pursue most worthwhile cases involving vulnerable groups. For those few cases in which a "reasonable in the circumstances" test is inadequate, a statutory standard should allow the Commission to challenge ads that would injure vulnerable groups. In such cases, the Commission should be able to challenge advertising if it can show that the advertiser knew or should have known that the ad would mislead some consumers.

In appropriate cases, establishing that an advertiser knew or should have known of the consequences of his advertising should not be a difficult burden to meet. First, "knew or should have known" is not the normal criminal standard. It is much more akin to negligence; indeed, "should have known" is the classic tort phrase for negligence. The Commission need not prove that the advertiser intended the consequences of a particular communication; rather, it is enough to show that the advertiser should have realized the risk that those consequences would follow.

Second, the Commission has developed experience with this standard over the years. Some Commission decisions have applied it in assessing the liability of advertising agencies for false ads. The Commission finds liability by examining objective factors relating to the ad agency's degree of participation in the campaign. Moreover, all of the cases in the defects program except one have pled in the complaints that the manufacturer knew or should have known that the product was likely to experience a particular problem. An investigation considers the information about the problem that was available to the company at the time. Until now, the standard has not been thought to cause an insurmountable, or even a terribly difficult burden.

Finally, in many cases, the "knew or should have known" standard will probably not even require additional evidence. It can be argued, for example, that an advertiser should have realized that depicting children riding tricycles into the street could lead some children to believe that this behavior is safe. And, it seems clear that an advertiser should have realized the risk that children would imitate the child in an advertisement playing with a hair dryer near water, particularly because the advertised product was a doll with washable hair.

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[62] Cohen. Consumer Safety Net Starting to Unravel. Advertising Age, March 8, 1982. p. 28.

[63] Miller. Reauthorization of FTC, p. 8 (emphasis added).

[64] Kintner. A Primer on the Law of Deceptive Practices, p. 98.

In short, even with the proposed standard, the Commission will continue to be able to provide valuable protection to vulnerable groups, without a significant increase in the evidentiary burden. By using extreme examples to discourage the enactment of new standards, critics are really suggesting that evidence should not be essential before the Commission acts in cases when it is not clear there has been any wrong to correct. Quite the contrary, I believe that evidence will assure that the Commission acts only when it should.[65]

Con

As for the suggestion that the Commission prove that a company "knew or should have known" a practice affecting "vulnerable" groups was deceptive, I believe that an intent standard is certainly reasonable in a law that imposes monetary fines on an individual, and that standard already applies in the FTC Act where penalties are permitted. But the FTC Act is also remedial. It is designed to protect consumers from false advertising and other deceptive practices, not to punish business. The only relevant question in determining whether to challenge a practice should be whether the practice is deceptive, not whether the person engaged in it knows it is.

If a company is engaged in a compaign of false advertising, and this can be proven, it should not also be necessary for the government to show that the company should have known its advertising was false before the false ads can be halted. A businessperson's intent does not mitigate injury to customers and competitors caused by false advertising. Further, the knowledge standard could be read to mean that a businessperson could only know that his or her practices were deceptive if they had been challenged in some other context before. Thus, the change could have the effect of introducing an actual notice requirement into the law, thereby virtually freezing the development of consumer protection at the date of its enactment. Ironically, the adoption of this standard would make it more, rather than less difficult for the Commission to protect vulnerable groups.[66]

Another suggestion that has been made with respect to deception warrants not because it poses even more serious concerns. It has been suggested that in both the deception and unfairness areas that an intent element be incorporated into the law. The effect of such an element, of course, would be to permit forever the use of a challenged practice, regardless of the injury that it causes, if it cannot be demonstrated that the practice was initially used with knowledge or reason to know that it would violate Section 5 and cause economic or other injury to consumers. Once again, the different orientation and functions of public law and private law, from which the intent element is transported, must be taken into account. In that regard, I simply urge you to reflect upon the fact that the advertising industry trade publication. Printers Ink, concluded as far back as 1911—when it proposed a model statute for adoption by the States as the basis for redressing and preventing marketplace deception—that deception in the marketplace is injurious and wrong regardless of whether or not it is the result of intentional or knowing behavior. A rule that would permit even demonstrably evident actual deception or unfairness to be continued with impunity simply because its initial use was innocent would be a travesty on consumers and totally inconsistent with the efforts of Congress to secure to all the benefits of competitive, honest and fair market systems.[67]

(I)f the challenged advertising was directed at "vulnerable groups"—the poor, the elderly, and the uneducated—who might fall through the statutory category of "reasonable consumers," Miller would still give the Commission a shot at protecting them from deception if we are able to prove that the advertiser actually intended to deceive or that the reasonable advertiser should have known that his ad was deceptive. A mens rea requirement has never been an element of deception under Section 5, and appropriately not. The FTC Act is not a criminal statute. It does not punish the sinner, it simply seeks to protect the consumer. Intent is irrevelant to whether consumers may be injured and, consequently, to whether a company should be ordered to cease and desist from deceiving the public. Moreover, intent is enormously difficult to prove. Therefore, while Miller's proposal purports to provide special protection for vulnerable groups, the impact of his proposal would leave such groups far more vulnerable to exploitation than under present law.[68]

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[65] Muris Memo. Reauthorization of FTC, p. 70–71.

[66] Bailey. Reauthorization of FTC, p. 355.

[67] Professor Rice. Reauthorization of FTC, p. 259.

[68] Pertschuk. Reauthorization of FTC, p. 224.

Finally, I doubt that any business which has been investigated for an alleged violation involving intent as an element would—given the inevitability of an FTC investigation into its trade practices—prefer to have the kind of investigation that accompanies an enforcement agency's attempts to prove intent. Inquiries (some using compulsory process) of customers, employees, family, business associates and others may become fair game when the government seeks to prove what the business person knew and when he knew it. While the number of investigations probably would decrease because of the greater resources needed to show intent, those who were investigated would probably regret that intent was a relevant issue.[69]

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[69] Silbergeld. Reauthorization of FTC, p. 155.